## Before the Federal Communications Commission Washington, D.C. 20554

In the Matter of	)	
Applications of	)	
Applications of	)	
Comcast Corp.,	)	
Time Warner Cable, Inc.	)	MB Docket No. 14-57
Charter Communications, Inc., and	)	
SpinCo	)	
	)	
For Consent to Transfer Control of	)	
Licenses and Authorizations	)	



### **COMMENTS**

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### **EXECUTIVE SUMMARY**

In these comments, the American Cable Association ("ACA") demonstrates that the combination of the nation's two largest cable operators, Comcast Corp. ("Comcast") and Time Warner Cable Inc. ("TWC"), both of which have significant interests in video programming, and Comcast later divesting to and swapping systems with Charter Communications, Inc. ("Charter"), which also has attributable programming interests, will result in harm to competition and consumers, particularly in the multichannel video programming distribution ("MVPD") and programming markets. The program access remedies utilized in prior Commission transaction reviews involving similar combinations of programming and distribution assets are inadequate to address these public interest harms. Because these harms are so significant, and are not counterbalanced by public interest benefits, the Commission cannot approve the proposed combination without adopting specific and meaningful relief.

ACA has a substantial interest in this proceeding because its approximately 840 small and medium-sized member cable operators either acquire programming from Comcast or TWC, compete in the MVPD market with Comcast, TWC and Charter cable systems, or, in select instances, both acquire programming and compete in distribution. More specifically, today all ACA members transact, directly or indirectly, with the Applicants and their affiliates for distribution rights to consumers and access to broadcast and cable programming networks.

These transactions include deals for carriage of "must have" programming, including NBC network broadcast programming aired on local owned and operated ("O&O") broadcast stations, Comcast and TWC regional sports networks ("RSNs"), and suites of NBCUniversal (NBCU) cable programming networks such as USA Network, CNBC, Golf Channel, Syfy, Bravo, E!, MSNBC, and other core programming. Further, dozens of ACA members compete directly with

Comcast, TWC and Charter cable systems, some in multiple markets – small companies going head-to-head with the nation's largest cable MVPDs.

The Comcast-TWC-Charter transaction involves companies with significant roles in both the downstream MVPD industry and the upstream video programming industry. While it has been observed that the "vast majority of mergers are either procompetitive and enhance consumer welfare or are competitively benign," the Comcast-TWC-Charter transaction is neither. ACA will demonstrate that the proposed transaction, if consummated, will have significant deleterious vertical and horizontal competitive effects.

Vertical Harm. The proposed integration of Comcast's valuable programming assets and TWC's distribution systems exacerbates the harm the Commission and the U.S. Department of Justice ("DOJ") found in the Comcast-NBCU merger by uniting substantial video programming and distribution assets. The Commission recognized that once joined, Comcast-NBCU would negotiate more aggressively relative to pre-transaction NBCU when selling NBCU content to Comcast's video distribution rivals because the integrated firm would take into account the possibility that any harm from failure or delay in reaching agreement would be offset to some extent by a benefit to Comcast, as reaching a higher price would raise the costs of Comcast's rivals. By improving Comcast-NBCU's bargaining position, the transaction would lead to higher programming costs for Comcast's video distribution rivals. Once it acquires cable systems from TWC and Charter, this very same harm will be magnified by the increased overlap of Comcast's territory with rival MVPDs, and will increase Comcast's incentives and ability to command higher programming fees from MVPDs that compete with Comcast. Charter's growth will inflict similar harms to its rival MVPDs.

The existing vertical harm will grow larger in two ways. First is the increased opportunity of attracting subscribers from rival MVPDs due to the increased number of homes passed by Comcast. Second is the increased profit of attracting new subscribers due to the efficiencies the Applicants claim will be created by the merger. The resulting fee increases may be substantially passed through to subscribers in the form of higher subscription fees.

Additionally, vertical price effects will also be felt by Comcast's own subscribers in the form of increased prices as the combined entity profits from the sale of programming to rivals even if it loses some subscribers due to price increases, leading to widespread general public interest harm through increased prices.

**Horizontal Harms.** The transaction threatens two sets of horizontal harms. The first concerns the addition of TWC's RSNs in Los Angeles and New York to the vast array of programming offered by Comcast. The second concerns the increased bargaining power with respect to its programming that Comcast will attain by increasing its subscriber base from 21.1 million to up to 31.4 million video subscribers (to the extent Comcast negotiates on behalf of Bright House Networks and Midcontinent).

Horizontal Harm from the Combination of Comcast and TWC Programming Assets.

This horizontal harm arises from the proposed transaction when key programming assets of Comcast and TWC are joined post-transaction into one powerful company. More specifically, today Comcast and TWC each own video programming assets. Comcast owns NBCU O&O stations, national cable programming networks and RSNs. TWC owns several RSNs. Through the acquisition of TWC, Comcast will acquire two RSNs in the two largest media markets and cities in the country, Lost Angeles and New York. By combining control of these assets, Comcast will have an increased incentive and ability to command higher prices for this

programming, especially in markets where MVPDs distribute both a Comcast RSN and an NBC O&O, resulting in harm to MVPDs and consumers. The Commission has recognized that horizontal integration of programming assets gives a company greater bargaining power to extract higher rates from MVPDs in both the *Comcast-NBCU Order* and in its recent retransmission consent reform rulemaking. The result will be no different in this case.

<u>Increased Horizontal Scale of Comcast</u>. The proposed combination will also result in horizontal harm from an increase in Comcast's bargaining and purchasing power in programming markets. In the cable television industry, programmers traditionally offer volume discounts based on the number of subscribers an MVPD serves. Post-transaction, programmers will be negotiating with an MVPD that holds nearly one third of subscribers across the country. Prior to the transaction, Comcast was the largest MVPD in the country, and TWC the second largest cable operator – each able to command the best and most competitive rates from programmers. Post-transaction, Comcast will have increased bargaining power over these programmers and will have the ability to receive the lowest rates possible. Charter's growth will result in it receiving lower rates as well. Accordingly the disparity in programming fees paid by the largest cable operators compared to their small rivals will expand, and become more competitively troublesome. Comcast's and Charter's increased bargaining power will also lead programmers to recoup these losses from other MVPDs by charging them higher and less competitive prices. Further, by obtaining lower prices, Comcast will increase its profitability per subscriber, which will lead to an increase in the opportunity cost for Comcast to sell its programming to rival MVPDs, and, in turn, lead to higher Comcast programming costs for these MVPDs. ACA members will be threatened the most in these circumstances.

Harm in Advertising Markets. The proposed combination will also lead to public interest harms in the spot cable advertising market. Post-acquisition, Comcast will have increased control and leverage in the NCC, regional Interconnects and in spot cable advertising representation services. This increased control, across all aspects of the spot cable advertising market, will give Comcast another lever to raise the costs of its competitors and subsequently harm consumers.

Arbitration Conditions are Inadequate to Address Harms. Previous remedies utilized by the Commission, including baseball-style arbitration, are not adequate to alleviate the public interest harms raised by this combination, particularly for small and medium-sized MVPDs. In any baseball-style arbitration proceeding, small and mid-sized MVPDs are disadvantaged by multiple factors, including a lack of critical information and information imbalance in the arbitration process, the high fixed costs of the arbitration process, threat of retaliation from programmers and problems starting the process. These short-comings must be addressed in any remedial conditions imposed on the Applicants as a condition of grant of their license transfers.

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### **COMMENTS**

The American Cable Association ("ACA") submits these comments in response to the Public Notice issued by the Commission in the above captioned proceeding on July 18, 2014 seeking comment on applications filed by Comcast Corporation ("Comcast"), Time Warner Cable Inc. ("TWC"), Charter Communications, Inc. ("Charter") and SpinCo (collectively, "the Applicants") seeking consent to transfer control of various Commission licenses and other authorizations associated with a series of transactions that will vastly augment the size and reach of Comcast, the nation's largest cable operator through its absorption of TWC, the second largest

operator, and significantly increase the size of Charter, the nation's fourth largest cable operator.<sup>1</sup> ACA maintains, and will demonstrate, that the transactions between and among the Applicants will, by increasing Comcast's total number of homes passed through its acquisition of TWC and Charter systems and by adding TWC's programming to Comcast's already prodigious suite of programming assets, adversely affect a majority of the multichannel video programming distributor ("MVPD") subscribers served by other distributors who compete against Comcast as well as harm Comcast's own customers, contrary to the public interest. Furthermore, the transaction will, by increasing both Comcast's and Charter's total numbers of subscribers served, increase their bargaining leverage with programmers and result in these companies lowering their overall programming costs. This outcome will further increase the disparity in the wholesale programming rates paid by these large cable operators and their smaller rivals. In these comments, which include an extensive economic analysis by Professor Gary Biglaiser, ACA describes these harms in detail and with evidentiary support, and provides a critique of the effectiveness of prior Commission remedial conditions to ameliorate these harms for smaller and medium-sized MVPDs.<sup>2</sup> Unless the Commission adopts robust relief to remedy the transactions' harms, these deals should not be approved.

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<sup>&</sup>lt;sup>1</sup> Public Notice, Commission Seeks Comment on Applications of Comcast Corporation, Time Warner Cable Inc., Charter Communications, Inc., and SpinCo To Assign and Transfer Control of FCC Licenses and Other Authorizations, MB Docket No. 14-57, DA 14-96 (rel. Jul. 10, 2014) ("Public Notice").

<sup>&</sup>lt;sup>2</sup> See Gary Biglaiser, The Harms of Comcast-TWC-Transaction (August 25, 2014), attached hereto as Exhibit A ("Biglaiser").

### I. INTRODUCTION

Because its approximately 840 small and medium-sized member cable operators either acquire programming from Comcast or TWC, compete in the MVPD market with Comcast, TWC and Charter cable systems, or, in select instances, both acquire programming and compete in distribution, ACA has a substantial interest in this proceeding. More specifically, today all ACA members transact, directly or indirectly, with the Applicants and their affiliates for distribution rights to consumers and access to broadcast and cable programming networks.

These transactions include deals for carriage of "must have" programming, including NBC network broadcast programming aired on local owned and operated ("O&O") broadcast stations, Comcast and TWC regional sports networks ("RSNs"), and suites of NBCUniversal (NBCU) cable programming networks such as USA Network, CNBC, Golf Channel, Syfy, Bravo, E!, MSNBC, and other core programming. Further, dozens of ACA members compete directly with Comcast, TWC and Charter cable systems, some in multiple markets – small companies going head-to-head with the nation's largest cable MVPDs.

While it has been observed that the "vast majority of mergers are either procompetitive and enhance consumer welfare or are competitively benign," the Comcast-TWC-Charter transaction is neither.<sup>3</sup> ACA will demonstrate that the proposed transaction, if consummated, will have significant deleterious vertical and horizontal competitive effects. As a result of this transaction, Comcast will have an increased incentive and ability to extract supra-competitive prices for its video programming from other MVPDs and these rate increases will be

<sup>&</sup>lt;sup>3</sup> Christine A. Varney, Merger Guideline Workshops, Third Annual Georgetown Law Global Antitrust Enforcement Symposium (September 22, 2009), available at: http://www.justice.gov/atr/public/speeches/250238.pdf.

substantially passed through to subscribers in the form of higher subscription fees. The combination of Comcast and TWC will exacerbate the vertical harms created through the merger of Comcast and NBCU by giving Comcast an increased and geographically-expanded subscriber base. Vertical price effects will also be felt by Comcast's own subscribers in the form of increased prices as the combined entity profits from the sale of programming to rivals even if it loses some subscribers due to price increases, leading to widespread general public interest harm through increased prices.

The transaction also risks two sets of horizontal harm. The first concerns the addition of TWC's RSNs in Los Angeles and New York to Comcast's vast array of high value programming, particularly its NBC O&Os in those markets. Comcast's acquisition of a second block of must have programming to add to its NBC O&O stations in the two largest cities and media markets in the country will give it increased incentive and ability to command supra-competitive prices by combining negotiations for its programming assets, particularly for retransmission consent and RSN carriage.<sup>4</sup>

The second horizontal harm arises from the increased economic power of a far larger Comcast. ACA believes that Comcast will have increased purchasing power and ability to command the best rates from programmers by growing from 21.1 to 31.4 million subscribers (to the extent Comcast negotiations on behalf of Bright House Networks and Midcontinent). And programmers will seek to recoup these losses from small and mid-size MVPDs. Charter's

<sup>&</sup>lt;sup>4</sup> The Commission accepted the two separately owned broadcast station in the same DMA could extract higher prices than either could obtain by negotiating separately in its recent decision to prohibit joint negotiations as a per se violation of the duty to negotiate retransmission consent in good faith. *Amendment of the Commission's Rules Related to Retransmission Consent*, Report and Order and Further Notice of Proposed Rulemaking, MB Docket No. 10-71, (rel. Mar. 31, 2014), ¶ 6.

growth will have a similar affect. Comcast will also have increased control over the spot cable advertising and spot cable advertising representation markets, to the detriment of competition.

Previous remedies proposed by the Commission, including baseball-style arbitration, are not adequate to alleviate the harms raised by this combination, particularly for small and midsized MVPDs. In any baseball-style arbitration proceeding, small and mid-sized MVPDs are disadvantaged by multiple factors, including a lack of critical information and information imbalance in the arbitration process, the high fixed costs of the arbitration process, threat of retaliation from programmers and problems starting the process. Unless the Commission adopts robust relief to remedy the transactions' harms, these deals should not be approved.

In the following sections, the ACA will describe these harms in detail, providing evidence in support of their existence and magnitude.

#### II. STANDARD OF REVIEW

Under Section 310(d) of the Communications Act,<sup>5</sup> the Federal Communications Commission ("FCC" or "Commission") must determine whether the Applicants have demonstrated that the proposed assignment and transfer of control of certain FCC licenses and authorizations held by Comcast and TWC as part of the proposed transaction will serve "the public interest, convenience, and necessity." In making this determination the Commission

<sup>&</sup>lt;sup>5</sup> 47 U.S.C. § 310(d).

<sup>&</sup>lt;sup>6</sup> Section 310(d) of the Act, 47 U.S.C. § 310(d), requires that the Commission consider applications for transfer of Title III licenses under the same standard as if the proposed transferee were applying for licenses directly under Section 308 of the Act, 47 U.S.C. § 308. See, e.g., Applications of Comcast Corp., General Electric Co. and NBC Universal, Inc. for Consent to Assign Licenses and Transfer Control of Licensees, MB Docket No. 10-56, Memorandum Opinion and Order, 26 FCC Rcd 4238, 4247, ¶ 22 (2011) ("Comcast-NBCU Order"); Applications for Consent to the Transfer of Control of Licenses, XM Satellite Radio Holdings Inc., Transferor, To Sirius Satellite Radio Inc., Transferee, MB Docket No. 07-57, Memorandum

must first assess whether the proposed transaction complies with the specific provisions of the Act, other applicable statutes, and the Commission's rules. If the proposed transaction would not violate a statute or rule, the Commission next must consider whether it could result in public interest harms by substantially frustrating or impairing the objectives or implementation of the Communications Act or related statutes.<sup>7</sup> The Commission then employs a balancing test weighing any potential public interest harms of the proposed transaction against any potential public interest benefits.<sup>8</sup> The Applicants bear the burden of proving, by a preponderance of the

Opinion and Order, 23 FCC Rcd 12348, 12363, ¶ 30 (2008) ("XM-Sirius Order"); News Corp. and DIRECTV Group, Inc. and Liberty Media Corp. for Authority to Transfer Control, 23 FCC Rcd 3265, 3276, ¶ 22 (2008) ("Liberty Media-DIRECTV Order"); Applications for Consent to the Assignment and/or Transfer of Control of Licenses Adelphia Communications Corporation, (and subsidiaries, debtors-in-possession), Assignors, to Time Warner Cable Inc. (subsidiaries), Assignees; Adelphia Communications Corporation, (and subsidiaries, debtors-in-possession), Assignors and Transferors, to Comcast Corporation (subsidiaries), Assignees and Transferees; Comcast Corporation, Transferor, to Time Warner Inc., Transferee; Time Warner Inc., Transferor, to Comcast Corporation, Transferee, Memorandum Opinion and Order, 21 FCC Rcd 8203, ¶ 23 (2006) ("Adelphia Order"); SBC Comm. Inc. and AT&T Corp. Applications for *Approval of Transfer of Control*, 20 FCC Rcd 18290, 18300, ¶ 16 (2005) ("SBC-AT&T Order"); Verizon Comm., Inc. and MCI, Inc. Applications for Approval of Transfer of Control, 20 FCC Rcd 18433, 18443, ¶ 16 (2005) ("Verizon-MCI Order"); General Motors Corporation and Hughes Electronics Corporation, Transferors, and The News Corporation Limited, Transferee, MB Docket No. 03-124, Memorandum Opinion and Order, 19 FCC Rcd 473, 485, ¶ 18 (2004) ("News Corp.-Hughes Order"). See also SkyTerra Communications, Inc., Transferor and Harbinger Capital Partners Funds, Transferee Applications for Consent to Transfer of Control of SkyTerra Subsidiary, LLC, IB Docket No. 08- 184 et al., Memorandum Opinion and Order and Declaratory Ruling, DA 10-535, ¶ 10 (rel. Mar. 26, 2010).

<sup>7</sup> See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4247, ¶ 22; XM-Sirius Order, 23 FCC Rcd at 12364, ¶ 30; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3276-77 ¶ 22; SBC-AT&T Order, 20 FCC Rcd at 18300, ¶ 16; Verizon-MCI Order, 20 FCC Rcd at 18443, ¶ 16.

<sup>&</sup>lt;sup>8</sup> See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4247,  $\P$  22; XM-Sirius Order, 23 FCC Rcd at 12364,  $\P$  30; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3277,  $\P$  22; SBC-AT&T Order, 20 FCC Rcd at 18300,  $\P$  16; Verizon-MCI Order, 20 FCC Rcd at 18443,  $\P$  16; News Corp.-Hughes Order, 19 FCC Rcd at 483,  $\P$  15.

evidence, that the proposed transaction, on balance, will serve the public interest. 9 If the Commission is unable to find that the proposed transaction serves the public interest for any reason, or if the record presents a substantial and material question of fact, the application must be designated for hearing.<sup>10</sup>

The Commission's public interest evaluation necessarily encompasses the "broad aims of the Communications Act,"11 which include, among other things, "a deeply rooted preference for preserving and enhancing competition in relevant markets, accelerating private-sector deployment of advanced services, ensuring a diversity of information sources and services to the public, and generally managing spectrum in the public interest."<sup>12</sup> The Commission's public interest analysis may also entail assessing whether the transaction will affect the quality of

 $<sup>^9</sup>$  See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4247,  $\P$  22; XM-Sirius Order, 23 FCC Rcd at 12364, ¶ 30; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3277 ¶ 22; SBC-AT&T Order, 20 FCC Rcd at 18300, ¶ 16; Verizon-MCI Order, 20 FCC Rcd at 18443, ¶ 16; Application of EchoStar Communications Corporation (a Nevada Corporation), General Motors Corporation, and Hughes Electronics Corporation (Delaware Corporations) (Transferors) and EchoStar Communications Corporation (a Delaware Corporation) (Transferee), CS Docket No. 01-348, Hearing Designation Order, 17 FCC Rcd 20559, 20574, ¶ 25 (2002) ("EchoStar-DirecTV" Order").

<sup>&</sup>lt;sup>10</sup> 47 U.S.C. § 309(e); see also Comcast-NBCU Order, 26 FCC Rcd at 4248, ¶ 22; XM-Sirius Order, 23 FCC Rcd at 12364, ¶ 30; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3277, ¶ 22; Adelphia Order, 21 FCC Rcd at 8217-18\_¶ 23; SBC-AT&T Order, 20 FCC Rcd at 18300, ¶ 16; Verizon-MCI Order, 20 FCC Rcd at 18443, ¶ 16; EchoStar-DirecTV Order, 17 FCC Rcd at 20574, ¶ 25.

<sup>&</sup>lt;sup>11</sup> See. e.g., Comcast-NBCU Order, 26 FCC Rcd at 4248, ¶ 23; XM-Sirius Order, 23 FCC Rcd at 12364, ¶ 31; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3277 ¶ 23; News Corp.-Hughes Order, 19 FCC Rcd at 483, ¶ 16; EchoStar-DIRECTV Order, 17 FCC Rcd at 20575, ¶ 26.

<sup>&</sup>lt;sup>12</sup> See Telecommunications Act of 1996, Pub. L. No. 104-104, § 706, 110 Stat. 56, 153 ("1996") Act"), codified at 47 U.S.C. § 157; 47 U.S.C. §§ 254, 332(c)(7); 1996 Act, Preamble; Comcast-NBCU Order, 26 FCC Rcd at 4248, ¶ 23; XM-Sirius Order, 23 FCC Rcd at 12365, ¶ 31; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3277-78, ¶ 23.

communications services or will result in the provision of new or additional services to consumers. <sup>13</sup> In conducting this analysis, the Commission may consider technological and market changes as well as trends within the communications industry, including the nature and rate of change. <sup>14</sup>

The Commission's competitive analysis, which forms an important part of the public interest evaluation, is informed by, but not limited to, traditional antitrust principles. The Commission and the DOJ each have independent authority to examine the competitive impacts of proposed communications transactions involving transfers of Commission licenses, but the standards governing the Commission's competitive review differ somewhat from those applied by the DOJ. Like the DOJ, the Commission considers how a transaction will affect competition by defining a relevant market, looking at the market power of incumbent competitors, and analyzing barriers to entry, potential competition and the efficiencies, if any, that may result from the transaction. The DOJ's review, however, focuses on whether a

 $<sup>^{13}</sup>$  See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4248,  $\P$  23; XM-Sirius Order, 23 FCC Rcd at 12365,  $\P$  31; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3277-78,  $\P$  23.

 $<sup>^{14}</sup>$  See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4248,  $\P$  23; XM-Sirius Order, 23 FCC Rcd at 12365,  $\P$  31; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3277-78,  $\P$  23.

<sup>&</sup>lt;sup>15</sup> See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4248, ¶ 24; XM-Sirius Order, 23 FCC Rcd at 12365, ¶ 32; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3278, ¶24; Adelphia Order, 21 FCC Rcd at 8218, ¶ 25; News Corp.-Hughes Order, 19 FCC Rcd at 484, ¶ 17; EchoStar-DIRECTV Order, 17 FCC Rcd at 20575, ¶ 27.

<sup>&</sup>lt;sup>16</sup> See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4248, ¶ 24; XM-Sirius Order, 23 FCC Rcd at 12365, ¶ 32; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3278, ¶ 24; Verizon-MCI Order, 20 FCC Rcd at 18444, ¶ 18; SBC-AT&T Order, 20 FCC Rcd at 18302 ¶ 18. See also Satellite Business Systems, 62 FCC 2d 997, 1088 (1977), aff'd sub nom. United States v. FCC, 652 F.2d 72 (D.C. Cir. 1980) (en banc); Northern Utilities Service Co. v. FERC, 993 F.2d 937, 947-48 (1st Cir. 1993) (public interest standard does not require agencies "to analyze proposed mergers under the same standards that the Department of Justice . . . must apply").

transaction may substantially lessen competition or tend to create a monopoly.<sup>17</sup> Under the Commission's review, the Applicants must show that the transaction affirmatively will serve the public interest; otherwise the application is set for hearing. Whereas the DOJ's review is also limited solely to an examination of the competitive effects of the acquisition, without reference to other public interest considerations, <sup>18</sup> the Commission's competitive analysis under the public interest standard is somewhat broader.

The Commission's analysis recognizes that a proposed transaction may lead to both beneficial and harmful consequences.<sup>19</sup> For instance, combining assets may allow a firm to reduce transaction costs and offer new products, but it may also create market power, create or enhance barriers to entry by potential competitors, and create opportunities to disadvantage rivals in anticompetitive ways.<sup>20</sup> The Commission's public interest authority enables it, where appropriate, to impose and enforce transaction-related conditions that ensure that the public interest is served by the transaction.<sup>21</sup>

Section 303(r) of the Communications Act authorizes the Commission to prescribe restrictions or conditions not inconsistent with law that may be necessary to carry out the

 $^{18}$  See, e.g., XM-Sirius Order, 23 FCC Rcd at 12366,  $\P$  32.

<sup>&</sup>lt;sup>17</sup> 15 U.S.C. § 18.

See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4249, ¶ 25; XM-Sirius Order, 23 FCC Rcd at 12366, ¶ 33; Adelphia Order, 21 FCC Rcd 8219, ¶ 25; SBC-AT&T Order, 20 FCC Rcd at 18302, ¶ 18; Verizon-MCI Order, 20 FCC Rcd at 18444-45, ¶ 18.

<sup>&</sup>lt;sup>20</sup> See, e.g., XM-Sirius Order, 23 FCC Rcd at 12366,  $\P$  33; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3278-79,  $\P$  25; Adelphia Order, 21 FCC Rcd 8219,  $\P$  25.

<sup>&</sup>lt;sup>21</sup> See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4249, ¶ 25; XM-Sirius Order, 23 FCC Rcd at 12366, ¶ 33; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3279, ¶ 26.

provisions of the Act.<sup>22</sup> Indeed, unlike the role of antitrust enforcement agencies, the Commission's public interest authority enables it to rely upon its extensive regulatory and enforcement experience to impose and enforce conditions to ensure that the transaction will yield overall public interest benefits.<sup>23</sup> Further, the Commission has held that it will impose conditions to confirm specific benefits or remedy specific harms likely to arise from the transaction and that are related to the Commission's responsibilities under the Act and related statutes.<sup>24</sup>

For the reasons explained below, on balance, the proposed transaction threatens significant public interest harms that are not outweighed by the projected public interest benefits of the combination. Accordingly, should the Applicants fail to offer means of addressing these threatened harms, the Commission must consider the imposition of conditions, beyond those imposed in previous transactions, to ensure that the transaction will be, on balance, consistent with the public interest.

<sup>&</sup>lt;sup>22</sup> 47 U.S.C. § 303(r); *see also Comcast-NBCU Order*, 26 FCC Rcd at 4249, ¶ 25; *XM-Sirius Order*, 23 FCC Rcd at 12366, ¶ 33; *Liberty Media-DIRECTV Order*, 23 FCC Rcd at 3279, ¶ 26; *U.S. v. Southwestern Cable Co.*, 392 U.S. 157, 178 (1968) (holding that section 303(r) permits the Commission to order a cable company not to carry broadcast signal beyond station's primary market); *United Video, Inc. v. FCC*, 890 F.2d 1173, 1182-83 (D.C. Cir. 1989) (affirming syndicated exclusivity rules adopted pursuant to section 303(r) authority). Similarly, Section 214(c) of the Act authorizes the Commission to attach to the certificate "such terms and conditions as in its judgment the public convenience and necessity may require." 47 U.S.C. § 214(c); *see also SBC-AT&T Order*, 20 FCC Rcd at 18303 ¶ 19; *Verizon-MCI Order*, 20 FCC Rcd at 18445, ¶ 19.

<sup>&</sup>lt;sup>23</sup> See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4249, ¶ 25; XM-Sirius Order, 23 FCC Rcd at 12366, ¶ 33; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3279 ¶ 26; News Corp.-Hughes Order, 19 FCC Rcd at 477, ¶ 5; see also Schurz Communications, Inc. v. FCC, 982 F.2d 1043, 1049 (7th Cir. 1992) (discussing Commission's authority to trade off reduction in competition for increase in diversity in enforcing public interest standard).

<sup>&</sup>lt;sup>24</sup> See, e.g., Comcast-NBCU Order, 26 FCC Rcd at 4249, ¶ 25; Liberty Media-DIRECTV Order, 23 FCC Rcd at 3279 ¶ 26; SBC-AT&T Order, 20 FCC Rcd at 18303, ¶ 19; Verizon-MCI Order, 20 FCC Rcd at 18445, ¶ 19.

# III. THE PROPOSED TRANSACTION THREATENS SERIOUS PUBLIC INTEREST HARMS

A. The Transaction Unites Substantial Video Programming and Distribution Assets.

The Comcast-TWC-Charter deal involves companies with significant roles in both the downstream video distribution (MVPD) industry, and the upstream video programming industry, which provides this programming to the MVPDs. Comcast is a media and technology giant with two primary businesses – Comcast Cable and NBCU. Comcast Cable today provides video, broadband Internet and other services and technologies through cable systems which serve approximately 21.1 million video customers. Comcast Cable also provides local, regional and national advertising services through Comcast Spotlight. Comcast Spotlight provides these services in approximately 80 markets. Comcast is also an owner of NCC Media, which represents national spot advertising sales across the country.

NBCU, which is owned and controlled by Comcast, operates the NBC and Telemundo broadcast television networks, including ten local O&O NBC television stations and 17 local O&O Telemundo stations. NBCU's cable national cable networks include Bravo, CNBC, E!, Esquire Network, Golf Channel, MSNBC, NBC Sports Network, Oxygen, Syfy, and USA Network, among others. Several regional sports networks (RSNs) are also part of NBCU's cable programming offerings, including RSNs in Houston, Chicago, Philadelphia, New England, and California, among others.

TWC also provides video, broadband Internet and other services and technologies through cable systems across the country. TWC's cable systems serve approximately 11.4 million video customers. TWC also owns and manages a number of local news channels, local lifestyle channels, local sports channels and a number of RSNs. TWC also sells video

advertising to local, regional and national customers. Along with Comcast and Cox, TWC is also an owner of NCC Media.

Charter Communications is the fourth-largest domestic cable operator. The company also provides broadband Internet and voice services. It has approximately 4.2 million residential video customers. Liberty Media has held a controlling interest in Charter since early 2013.

Because media executive John Malone holds a substantial interest in Charter through his stake in Liberty Media, and in cable programmers Discovery Communications and Starz, the Discovery Communications and Starz networks are considered attributable to Charter pursuant to the Commission's attribution rules. Popular networks deemed attributable to Charter under FCC rules include Discovery Channel, TLC, Animal Planet, The Oprah Winfrey Network, and Starz.

In the two proposed interrelated transactions (referred to herein as "transaction"),

Comcast will acquire 100 percent of TWC's equity and its 11.4 million customers. Comcast will
then divest TWC systems serving approximately 1.5 million existing subscribers directly to

Charter; (2) Comcast and Charter will transfer assets, respectively serving approximately 1.5

million existing TWC customers and 1.6 million Charter customers, thereby enhancing the
geographic clustering of both companies; and (3) Comcast will form and spin off to its
shareholders a new, independent, publicly-traded company ("SpinCo") that will operate systems

<sup>&</sup>lt;sup>25</sup>Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Fifteenth Report, MB Docket No. 12-203 (rel. Jul. 22, 2013), Appendix B, National Programming Services, Table B-1 (listing Liberty Media-affiliated programming networks).

serving approximately 2.5 million existing Comcast customers. Charter will acquire a one-third interest in SpinCo's equity, and enter into a services agreement with it.<sup>26</sup>

Thus, the proposed transaction involves both a horizontal combination of programming assets from Comcast and TWC and a vertical integration of these assets with Comcast, TWC and Charter distribution assets. The Commission has previously found it necessary to impose additional transaction-specific safeguards as conditions for approving vertical transactions between MVPDs and video programing networks. The record in those proceedings, including most recently the Comcast-NBCU proceeding, "supported allegations that the vertical integration of certain video programming networks with a particular MVPD would harm competition and enhance the integrated MVPD's market power despite the Commission's [program access] rules."<sup>27</sup> The categories of such "marquee" or "must have" programming the Commission recognized with respect to Comcast "includes a broad portfolio of national cable programming in addition to RSN and local broadcast programming." <sup>28</sup> The Commission found that "such programming is important to Comcast's competitors and without good substitutes from other sources;" loss of access to the programming would likely cause other MVPDs to lose subscribers, and, most importantly, that "the transaction will improve Comcast-NBCU's bargaining position, leading to an increase in programming costs for Comcast's video distribution rivals."<sup>29</sup> The

<sup>&</sup>lt;sup>26</sup> Under the agreement, SpinCo has the right to have Charter purchase programming on its behalf.

<sup>&</sup>lt;sup>27</sup> Comcast-NBCU Order, 26 FCC Rcd at 4253-4254, ¶ 35.

<sup>&</sup>lt;sup>28</sup> Comcast-NBCU Order, 26 FCC Rcd at 4254, ¶ 36.

<sup>&</sup>lt;sup>29</sup> *Comcast-NBCU Order*, 26 FCC Rcd at 4254-4255, ¶¶ 36, 37. The Commission had previously recognized that ownership of local broadcast television stations by one of the top four national broadcast networks conveyed "significant market power." *News Corp.-Hughes Order*,

Commission's findings are echoed by those of the U.S. Department of Justice ("DOJ") which similarly found that by acquiring control over NBCU programming, Comcast would gain significant market power and new incentives for engaging in discriminatory practices against downstream rivals through its "control of an important portfolio of current and library content" that rivals need to be in the business.<sup>30</sup>

Access to such "must have" programming by other MVPDs is at issue in the instant transaction as well. The combination of Comcast and TWC must have programming assets with the expanded reach of Comcast's cable systems post-transaction will exacerbate the competitive harms of the Comcast-NBCU merger, not only for MVPDs competing directly with Comcast and Charter, but for Comcast's own subscribers. The Applicants claim that the proposed transaction

19 FCC Rcd at 565, ¶ 201 ("We find that News Corp. currently possesses significant market power in the DMAs in which it as the ability to negotiate retransmission consent agreements on behalf of local broadcast television stations.").

http://www.justice.gov/atr/cases/f266100/266158.pdf, ("Post-transaction, the [Joint Venture] would gain increased bargaining leverage sufficient to negotiate higher prices or withhold NBCU content from Comcast's MVPD competitors. Comcast's rival distributors would have to pay the increased prices or not carry the programming. In either case, the MVPDs likely would be less effective competitors to Comcast, and Comcast would be able to delay or otherwise substantially impede the development of [online video distributors] as alternatives to MVPDs. All of these activities could have substantial anticompetitive effect on consumers and the market. Because Comcast would face less competition from other video programming distributors, it would be less constrained in its pricing decisions and have a reduced incentive to innovate. As a result, consumers likely would be forced to pay higher prices to obtain their video content or receive fewer benefits of innovation. They would also have fewer choices in the types of content and providers to which they would have access, and there would be lower levels of investment, less experimentation with new models of delivering content, and less diversity in the types and range of product offerings."); Complaint at ¶ 47-51, 59-60 filed in *United States v. Comcast Corp.*, Civ. Action. 1:11-cv-00106 (D.D.C. dated Jan. 18, 2011),

http://www.justice.gov/atr/cases/f266100/266158.pdf (finding proposed transaction will likely eliminate or lessen competition in sale of video programming and increase prices for video programming distribution services while decreasing innovation and quality of these services)..

<sup>&</sup>lt;sup>30</sup> Competitive Impact Statement at 23-27, filed in *United States v. Comcast Corp.*, Civ. Action No. 1:11-cv-00106 (D.D.C. dated Jan. 18, 2011),

does not raise *any* competition concerns with respect to their increased buying power over programming or their market power in local television and cable programming markets. Specifically, they argue that "there is no plausible theory of competitive harm arising from the horizontal elements of the transaction" and "no plausible theory that the transaction will facilitate 'foreclosure' or other exclusionary conduct." This implausibly narrow view of the potential harms posed by the transaction should be given little credence.

# B. The Proposed Comcast-TWC-Charter Transaction Will Increase the Vertical Harms Caused by the Comcast-NBCU Merger.

The Commission has long recognized that vertical integration between MVPDs and programmers can result in competitive harms that are not remedied by the program access rules and therefore must be addressed through transaction-specific remedial conditions. As discussed above, the Commission came to a similar conclusion in the *Comcast-NBCU Order* where it noted that the combination of Comcast distribution and programming assets and NBCU programming assets gives Comcast an incentive and ability to charge competing MVPDs higher prices for its programming. There, the Commission was concerned both that Comcast would withhold programming from other distributors and that it would raise the prices for such programming, finding, with respect to the latter form of harm that:

Comcast-NBCU will negotiate more aggressively relative to pre-transaction NBCU when selling NBCU content to Comcast's video distribution rivals. Unlike the pre-transaction NBCU, the integrated firm will take into account the possibility that any harm from failure or delay in reaching agreement would be offset to some extent by a benefit to Comcast, as reaching a higher price would

<sup>&</sup>lt;sup>31</sup> Applications of Comcast Corp. and Time Warner Cable Inc. for Consent to Transfer Control of Licenses and Authorizations, Applications and Public Interest Statement, at 138-169 (filed Apr. 8, 2014) ("Application").

 $<sup>^{32}</sup>$  News Corp.-Hughes Order, 19 FCC Rcd at 508,  $\P$  71.

raise the costs of Comcast's rivals. As a result, the transaction will improve Comcast-NBCU's bargaining position, leading to an increase in programming costs for Comcast's video distribution rivals.<sup>33</sup>

This transaction exacerbates the very harm the Commission and the DOJ found posed by the Comcast-NBCU merger by vertically integrating Comcast's valuable programming assets with TWC's distribution systems, creating enhanced vertical integration beyond that created by the Comcast-NBCU transaction. The specific vertical harm arises from the increased overlap of Comcast's service territory with that of rival MVPDs. The transaction will increase Comcast's incentive and ability to use its programming assets to raise fees and harm competing MVPDs and their subscribers.

In the accompanying analysis, Professor Biglaiser demonstrates how the existing vertical harm grows larger in two ways. First is the increased opportunity of attracting subscribers from rival MVPDs due to the increased number of homes passed by Comcast as a result of its cable system acquisition. Second is the increased profit of attracting new subscribers due to the efficiencies created by the merger. "The higher opportunity cost for selling its programming due to the merger gives Comcast a greater incentive to raise the prices for its programming to rival MVPDs."

Professor Biglaiser uses the bargaining framework employed by other economists and the Commission in its analysis of the harms of the Comcast-NBCU transaction. This framework computes the opportunity cost that Comcast incurs by selling programming to a rival MVPD. "A higher opportunity cost for providing programming to a rival provides an incentive for Comcast

<sup>&</sup>lt;sup>33</sup> *Comcast-NBCU Order*, 26 FCC Rcd at 4254-4255, ¶ 37.

<sup>&</sup>lt;sup>34</sup> Biglaiser at 5.

to raise its price for that programming. This increased cost to rival MVPDs will be passed on, in whole or in part, to the rival MVPD's subscribers in terms of higher cable fees."<sup>35</sup>

Professor Biglaiser's analysis is also based on the standard discrete choice model:

When consumers are facing a decision about what product to purchase, they evaluate the intrinsic qualities of the products and the price of each product in their feasible set of choices. They then choose the product attribute/price combination that maximizes their utilities. A product's quality has features where all consumers may agree about the product's quality such as the reliability of the product, and features where consumers may have different rankings for the product's quality, such as the program offering. They first type of features are known as vertical features, while the second are known as horizontal or idiosyncratic features. ... When consumers are making their decision about which MVPD to subscribe to, they evaluate the offering's vertical and horizontal features or qualities and the prices for each service. An MVPD will have a larger market than an MVPD that offers a lower value for a large number of consumers.<sup>36</sup>

To evaluate the additional vertical harm caused by this acquisition, Professor Biglaiser looked at the competitive overlap of Comcast with both larger MVPDs and with ACA's smaller members.<sup>37</sup> The overlap with ACA members was computed by using as a proxy the post-transaction overlap with members of the National Cable Television Cooperative ("NCTC"), a buying group through which member companies purchase their programming and related services.<sup>38</sup> As a buying group, NCTC negotiates standardized master agreements with

<sup>&</sup>lt;sup>35</sup> Biglaiser at 7.

<sup>&</sup>lt;sup>36</sup> Biglaiser at 9.

<sup>&</sup>lt;sup>37</sup> This competitive overlap is calculated using the membership of the National Cable Television Cooperative, but excluding its four largest members who rarely participate in NCTC deals. See Declaration of Rick Fickle, President and Chief Executive Officer, NCTC, ¶¶ 5-6, attached hereto as Exhibit B ("Fickle Declaration").

<sup>&</sup>lt;sup>38</sup> Fickle Declaration, ¶¶ 3-4. Mr. Fickle explains that NCTC is a non-profit cooperative purchasing organization for its member companies that own and operate cable systems throughout the United States and its territories. NCTC currently has approximately 910 member

programmers and technology vendors. It acts as an interface between the vendor and individual MVPDs so that the vendor can deal with a single entity for purposes of negotiating contracts, determining technical standards, billing for payments, collecting payments, and marketing. <sup>39</sup> NCTC has master agreements with the vast majority of cable networks. Almost all small and medium-sized MVPDs are members of the NCTC and purchase a substantial share of the programming they distribute through the NCTC; the largest four members of the NCTC are not actively engaged in NCTC agreements aside from a few minor programming agreements and therefore are considered by NCTC to be inactive. <sup>40</sup> Apart from the four largest, many of NCTC's active members compete across the country with Comcast, TWC, and Charter. <sup>41</sup>

Professor Biglaiser shows that the competitive overlap with large MVPDs who currently compete with Comcast or will compete with Comcast after the deal increases. He correspondingly shows that Comcast's assumption of TWC's relationship with BHN will also lead to a greater competitive overlap. The combined change in competitive overlap will result in higher prices and harm to these MVPDs and their consumers. The competitive overlap with smaller operators who purchase a substantial share of their programming through NCTC will also {{

companies serving millions of multichannel video programming distributor (MVPD) subscribers. Members range in size from the largest serving a few million to the smallest serving "tens of" subscribers, with a median size of fewer than 1,500 subscribers.

<sup>&</sup>lt;sup>39</sup> Fickle Declaration, ¶ 4.

<sup>&</sup>lt;sup>40</sup> Fickle Declaration, ¶ 5.

<sup>&</sup>lt;sup>41</sup> Fickle Declaration, ¶ 6.

<sup>&</sup>lt;sup>42</sup> Biglaiser at 19.

MVPDs	Subs	Pre Merger	Post Merger	Difference	Competitive	Total
		Competitive	Competitive		Overlap	Difference
		Overlap	Overlap		with BHN	
		with	with			
		Comcast	Comcast			
DIRECTV	20.2M	{ {	{ {	{ {	3%	{{}}}
DISH	14.1M	{ {	{ {	<b>{ {</b>	3%	{{
Network						
NCTC	9.0M	{{	{{	{{	4%	{{
Verizon	5.4M	{{	{{	{{	7%	{{
AT&T <sup>43</sup>	5.9M	N/A	N/A	N/A	N/A	N/A

Professor Biglaiser also identifies an additional vertical price effect present, but not recognized by the Commission in its review of the Comcast-NBCU merger, that will be continued and enhanced by the instant transaction. He demonstrates that the vertical ownership of programming by Comcast harms not only subscribers of rival MVPDs, but also Comcast subscribers. Acquisition of the NBCU programming gave Comcast an incentive to raise prices to its own subscribers because post-merger, it profits even from subscribers departing as a result of its actions, who then subscribe to another MVPD, by selling the NBCU programming to those other MVPDs.

This effect will increase Comcast's incentive to raise its own subscription price, and is in addition to the increased opportunity cost effect previously identified with respect to the Comcast-NBCU merger. With this higher opportunity cost, Comcast will charge more for programming to its subscribers, but will experience less loss in profit due to subscriber defections. Thus, not only were Comcast's rivals hurt by the merger with NBCU, but Comcast's own subscribers were hurt.<sup>44</sup>

<sup>&</sup>lt;sup>43</sup> Due to lack of reliable data on the video footprint of AT&T U-verse's service, it is not possible to reach a conclusion about the competitive increase or decrease for its 5.9 million subscribers.

<sup>&</sup>lt;sup>44</sup> Biglaiser at 20.

From this Professor Biglaiser concludes that post-transaction, Comcast's incentive to raise its rivals' costs will increase due to its enlarged subscriber base, and that the pricing effects on Comcast customers will further increase as a direct result.<sup>45</sup>

Additionally, the efficiencies claimed by the parties in the application may also lead to increased prices for consumers. As explained by Professor Biglaiser, "the alleged efficiencies due to the merger will result in higher profit per Comcast subscriber. This will increase the opportunity cost to Comcast of providing programming to rival MVPDs in areas where it is acquiring systems and where its current systems exist and thus increase the cost of such programs." In conclusion, "the result of higher profitability per subscriber will increase Comcast's opportunity cost of selling its programming to competitors, which will lead to higher prices for competitors to buy Comcast's programming."

## C. The Proposed Transaction Threatens Two Types of Horizontal Harm

Two sets of horizontal harms are created by the merger of Comcast and TWC. The first concerns the addition of TWC's RSNs in Los Angeles and New York City to the vast array of programming offered by Comcast. The second concerns the increased bargaining power with respect to its programming that Comcast will attain by increasing its subscriber base from 21.1 million to up to 31.4 million video subscribers (to the extent Comcast negotiates on behalf of Bright House Networks and Midcontinent). By adding TWC's RSNs in the two largest media markets in the country, Los Angeles and New York, where Comcast also owns the NBC stations,

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<sup>&</sup>lt;sup>45</sup> Biglaiser at 20-21.

<sup>&</sup>lt;sup>46</sup> Biglaiser at 22.

<sup>&</sup>lt;sup>47</sup> Biglaiser at 22.

Comcast will be able to charge more for the pair of programming assets than Comcast and TWC could have charged for each programming asset when owned separately. Furthermore, by increasing its subscriber count by about 49%, Comcast will be able to obtain lower prices from programmers and this will increase Comcast's profit per subscriber and thus its opportunity cost of selling programming to rival MVPDs. This, in turn, will harm these MVPDs' subscribers.

# 1. Horizontal harm through the combination of key Comcast and TWC programming assets in Los Angeles and New York.

The Commission has repeatedly recognized that horizontal integration of programming can increase the rates paid by small and mid-size MVPDs. In the *Comcast-NBCU Order* it noted that the "ability of a company to obtain greater bargaining power because of a horizontal transaction is a well-established concern in antitrust enforcement." Continuing, the Commission cited evidence that "when a single entity controlled the local broadcast rights to multiple broadcast networks that entity was able to secure a substantial bargaining advantage in retransmission consent negotiations with the local MVPD, leading to an increase in retransmission consent fees of at least 20 percent." The Commission most recently utilized this bargaining theory in its decision to prohibit the collusive practice of separately owned broadcast stations in the same DMA jointly negotiating retransmission consent as contrary to the public interest. The basis for this decision rested upon its finding that, by coordinating their

 $^{48}$  Comcast-NBCU Order, 26 FCC Rcd at 4294,  $\P$  135.

 $<sup>^{49}</sup>$  Comcast-NBCU Order, 26 FCC Rcd at 4295,  $\P$  137.

<sup>&</sup>lt;sup>50</sup> Amendment of the Commission's Rules Related to Retransmission Consent, Report and Order and Further Notice of Proposed Rulemaking, 29 FCC Rcd 3351, 3358, ¶ 13 (2014). ("Joint Negotiation Order").

negotiations, broadcasters could suppress competition in local television markets and thereby command higher prices than each station could obtain by negotiating individually.<sup>51</sup>

Through the acquisition of TWC, Comcast will acquire two RSNs in the two largest cities in the country, Los Angeles and New York. As explained below and in the accompanying analysis by Professor Biglaiser, by combining control over Comcast's and TWC's must have RSNs, the post-transaction Comcast-TWC will have the ability to command higher prices for the programming, especially in markets where MVPDs distribute both a Comcast RSN and an NBC owned and operated station. The Commission recognized the possibility for this precise harm in the *Comcast-NBCU Order*, where it found that Comcast's ability to increase MVPDs' costs by negotiating for the same types of programming together would raise prices to consumers and weaken the ability of smaller MVPDs to compete, both significant public interest harms. 53

As Professor Biglaiser demonstrates, this combined ownership of key programming assets will further increase Comcast's post-transaction bargaining power and allow it to charge higher fees for this programming.<sup>54</sup> Professor Biglaiser notes that when a programmer and an MVPD negotiate the fee that the MVPD will pay the programmer, they are basically deciding how to divide the joint economic gains created from having the MVPD carry the programming. A programmer selling two different networks will be able to charge more by bundling the networks together, as long as the networks are substitutes in the sense that the marginal value of

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<sup>&</sup>lt;sup>51</sup>Joint Negotiation Order, 29 FCC Rcd at 3358, ¶13.

<sup>&</sup>lt;sup>52</sup> Biglaiser at 17.

<sup>&</sup>lt;sup>53</sup> Comcast-NBCU Order, 26 FCC Rcd at 4295, ¶ 135.

<sup>&</sup>lt;sup>54</sup> Biglaiser at 25.

either of the networks to the MVPD is lower conditioned upon already carrying the other network. For this analysis to hold, it is not required that the networks are close substitutes; rather, the analysis turns on "the fact that the value of additional networks has diminishing value to an MVPD."

The Commission agreed with this assessment in both the *Comcast-NBCU Order* and its retransmission consent reform rulemaking. In the merger review, the Commission examined the case of a Fox O&O and a Fox RSN in the same DMA under the joint ownership of News Corp relative to a control group of RSNs not under joint ownership with a broadcast station.<sup>56</sup> The Commission found "that joint ownership of these two types of programming assets in the same region allowed the joint venture to charge a higher price for the RSN relative to what would be observed if the RSN and the local broadcast affiliate were separately owned."<sup>57</sup> This result held for five years after the horizontal integration of the RSN and the owned and operated broadcast station.<sup>58</sup> The result will be no different once Comcast gains control of TWC's RSNs in Los Angeles and New York, and will be similarly contrary to the public interest.

## 2. Horizontal harm arising from the vastly increased horizontal scale of Comcast.

Similar to the harm that flows directly from the ownership by Comcast and TWC of programming, the combined firm's increased bargaining power has the potential, independently and in combination with its potential to leverage its ownership of key programming assets, to

<sup>56</sup> Biglaiser at 26.

<sup>&</sup>lt;sup>55</sup> Biglaiser at 26.

<sup>&</sup>lt;sup>57</sup> Comcast-NBCU Order, 26 FCC Rcd at 4399, Appendix B, ¶ 55.

 $<sup>^{58}</sup>$  Comcast-NBCU Order, 26 FCC Rcd at 4399, Appendix B,  $\P$  55.

damage small MVPDs. Whether or not its proposed divestitures to Charter cure direct antitrust issues related to that increased purchasing power, the effect of the transaction even with the divestitures appears likely to harm all small MVPDs.

As explained by Professor Biglaiser, in the cable television industry, programmers traditionally offer volume discounts based on the number of subscribers an MVPD serves.<sup>59</sup> Prior to the transaction, Comcast was the largest MVPD in the United States with approximately 21.1 million subscribers. Excluding the two DBS providers, TWC was the second largest cable operator, with approximately 11.4 million subscribers. As the first and second largest cable operators in the country, Comcast and TWC were able to command the best and most competitive rates from programmers. After the transaction and the proposed divestitures, a combined Comcast-TWC will have approximately 31.4 million video subscribers (to the extent Comcast negotiates on behalf of Bright House Networks and Midcontinent), giving Comcast more than 30% of video subscribers across the country. Charter, through the proposed divestiture of subscribers from Comcast, will become the second largest cable operator in the country, with 5.6 million video customers. Through the divestiture and creation of SpinCo, for whom Charter will offer programming negotiating services, Charter will also gain leverage as its programming negotiator. In short, the largest operators will have gotten larger relative to ACA's membership.

If the transaction is approved, programmers will be negotiating with an MVPD that holds approximately one third of subscribers nationwide. With this many subscribers, Comcast will be able to negotiate for even better rates, as programmers will be induced to accept these lower rates

<sup>59</sup> Biglaiser at 29.

to continue to get their programming in front of as many consumers as possible.<sup>60</sup> Further, as explained by Professor Biglaiser, by obtaining lower prices, Comcast will increase its profitability per subscriber, which will lead to an increase in the opportunity cost for Comcast to sell its programming to rival MVPDs, and, in turn, lead to higher Comcast programming costs for these MVPDs, increases which will in part be borne by subscribers.<sup>61</sup>

Professor Biglaiser also explains why Comcast's position that the transaction will not increase its market power as a programming purchaser is highly unlikely. After noting that Comcast's economists treat the programming market as if being a large buyer does not increase a firm's market power because no individual MVPD is essential for any give programmer or broadcaster to profitably be in the market, Professor Biglaiser explains:

Unfortunately, in the programming market it is well-known that larger MVPDs get much better programming rates than smaller ones. It flies in the face of reality to think that by enlarging, Comcast will gain no additional market power as a purchaser in the programming market. If Comcast lost market power, and had to pay higher prices, then this would be a very large incentive not to merge with TWC. The merger will lead to higher profitability per subscriber due to the lower costs of buying programs, and again, a higher opportunity cost for Comcast to selling its programs to its competitors. Furthermore, and most strikingly, if TWC and Comcast thought that the merger would mean paying higher programming prices, then they would not allow {{

}} This is another piece of evidence suggesting Comcast will get better pricing from programmers as a result of the transaction with TWC and Charter.<sup>63</sup>

In his Declaration, Rich Fickle, CEO and President of NCTC, explains his view that if the deal is approved, programming vendors will receive less value for their programming in the near

<sup>&</sup>lt;sup>60</sup> *See* Biglaiser at 29; Fickle Declaration, ¶ 7.

<sup>&</sup>lt;sup>61</sup> Biglaiser at 27.

<sup>&</sup>lt;sup>62</sup> Biglaiser at 27-28.

<sup>&</sup>lt;sup>63</sup> Biglaiser at 28.

term from the combined companies than they would receive if the companies remained under separate ownership and control.

First, to the extent permissible, Comcast will bring the TWC systems under its existing programming agreements where the per-subscriber price paid by Comcast is lower. This will result in the programmers receiving less revenue from the TWC systems than they receive today. Second, as a result of growing from 21.1 million to up to 31.4 million video subscribers (to the extent Comcast negotiates on behalf of Bright House Networks and Midcontinent), Comcast will be in a better position to harm programmers by withholding or threatening to withhold access to its increased subscriber base. Accordingly Comcast will be able to obtain lower programming prices from its programming suppliers. Third, as a result of Charter's subscriber base growing from 4.2 million to up to 8 million subscribers (to the extent it negotiates on behalf of SpinCo), Charter will also have more bargaining power against the programmers, and be able to command better rates, terms and conditions from programmers.

Based on his long experience in the industry, Mr. Fickle expects that, as a result of the ability of Comcast and Charter to pay less for programming, "the largest programming/media companies – which have significant bargaining leverage – will extract higher fees and more onerous terms and conditions from other MVPDs in the market and NCTC" and that the transaction will increase the already significant difference between programming fees paid by Comcast and those paid by NCTC members. Finally, he attests to the fact that he has witnessed this "seesaw" effect playing out in the marketplace today.

Currently, NCTC faces increased demands from programmers resulting from the concessions that they grant large MVPDs such as Comcast and TWC. Programmers acknowledge during negotiations with the NCTC their need to make up the revenue amounts they are not about to secure from Comcast, TWC or other large MVPDs. Specifically, some programmers have stated their intention to make up lost revenues resulting from their negotiations with Comcast, TWC or others directly through their agreements with NCTC members and other small MVPDs. There is no reason to believe that programmers won't continue to seek

<sup>&</sup>lt;sup>64</sup> Fickle Declaration, ¶ 7.

<sup>&</sup>lt;sup>65</sup> Fickle Declaration, ¶ 8.

concessions from NCTC to make up for the increase in lost revenues after the Comcast/TWC/Charter deal is approved. The Comcast/TWC/Charter merger will put programmers in an even worse position in their negotiations with Comcast and Charter. This is why I expect programmers to make up revenues on the backs of small cable operators in the event the Comcast/TWC merger is approved. 66

NCTC is not the only entity to believe that all MVPDs smaller than Comcast will be harmed by the transaction. As DISH Network, the second largest DBS providers and third largest MVPD, recently explained:

[A] combined Comcast/TWC will be able to exercise its enormous size to leverage programming content in anti-competitive ways. It will be able to extract lower prices from programmers, which, in turn, will force programmers to extract even higher rates from smaller pay-TV providers like DISH in order to compensate the programmers for lost revenue. And a combined Comcast/TWC will have the incentive and ability to restrict programmers' ability to grant digital rights to competing pay-TV and OTT video providers.<sup>67</sup>

The situation described by DISH will be even grimmer for the smallest MVPDs, who

have far less bargaining power and leverage than a distributor like DISH, even when purchasing their national cable programming through a buying group like the NCTC.<sup>68</sup> This theory is explained in additional detail by Professor Biglaiser.<sup>69</sup> With substantially fewer subscribers, the smallest MVPDs will be most vulnerable to increased costs. This is both a public interest harm, and a competitive harm where Comcast and the small MVPDs compete directly.

In such markets, ACA members are at the largest competitive disadvantage. Comcast will be able to offer its subscribers the lowest possible prices, because Comcast receives the most

<sup>&</sup>lt;sup>66</sup> Fickle Declaration, ¶ 9.

<sup>&</sup>lt;sup>67</sup> Applications of Comcast Corp. and Time Warner Cable, Inc. for Consent to Assign or Transfer Control of Licenses and Authorizations, DISH Network, Ex Parte Presentation, MB Docket No. 14-57, (Aug. 1, 2014).

<sup>&</sup>lt;sup>68</sup> Biglaiser at 14.

<sup>&</sup>lt;sup>69</sup> Biglaiser at 15-17.

favorable rates from programmers. Competing small MVPDs, who are forced to accept higher rates from programmers, will have to recoup these higher costs by raising prices to their subscribers, putting them at a competitive disadvantage as opposed to Comcast. The small and diverse members of ACA are threatened the most under these circumstances.

This concern is far from hypothetical. The median number of subscribers per member is less than 1,500, or less than a fraction of one percent of video subscribers nationwide. In the *Comcast-NBCU Order*, the Commission recognized the differences in bargaining power between the largest and smallest MVPDs. In some instances, programmers have admitted that they are forced to account for negotiations with Comcast, as it currently exists, when negotiating with smaller MVPDs. This forces the programmers to be even more rigid with small MVPDs, causing disruption to the negotiation process and raising the costs of the small MVPDs in order for the programmer to make up for lower profits. The larger Comcast gets, the more the existing problem is exacerbated. Through the Comcast-TWC-Charter transaction, the gap between the largest MVPDs and the smallest MVPDs widens significantly. The larger the gap between these competitors, the more likely that harm may result. This harm impacts competition in output upstream, and programmers and small MVPDs alike suffer.

# D. The Proposed Transaction Will Give Comcast Greater Control and Leverage to Disadvantage MVPD Rivals in Advertising Markets.

ACA members and other competing MVPDs will also be harmed through Comcast's increased control and leverage in the spot cable television advertising market. As analysts estimate that advertising will account for gross sales of \$5.08 billion in 2014, this is an important revenue source for MVPDs.

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<sup>&</sup>lt;sup>70</sup> Fickle Declaration, ¶ 9.

Today, Comcast and TWC each own, control or are involved with significant spot cable advertising representation organizations. All national advertisers place spot cable advertising through one national representation firm, the National Cable Communications ("NCC") which represents national spot advertising sales for cable, satellite, and telco programming distributors across the nation. Comcast, together with TWC and Cox Media, are owners of NCC.<sup>71</sup>

In addition, each regional advertiser places spot cable advertising through an "Interconnect" – a joint sales and technical integration entity comprised of MVPDs that serve a given DMA. Generally speaking, the Interconnect is managed, and therefore controlled, by the dominant MVPD in the DMA. In the top markets across the country, this is either Comcast or TWC.

Advertisers can place spot cable advertising, which is the most local advertising, through an MVPD directly or through its spot cable advertising representative. Comcast also owns Comcast Spotlight, the advertising sales division of Comcast Cable, which provides spot cable advertising representation services to competing MVPDs such as Verizon, AT&T, DISH, DirecTV, Wide Open West and RCN. TWC, through Time Warner Cable Media Sales, also sells video and online advertising to local customers and cable spot advertising representation to other MVPDs. These services allow smaller MVPDs to participate in ad sales more effectively and economically than they could on their own, by providing technical infrastructure and staff to run the advertising operations. In addition to Comcast and TWC, there are also independent providers of spot cable advertising representation services, such as Viamedia, Inc. ("Viamedia").

<sup>71</sup> Application at 11.

<sup>72</sup> Application at 16.

MVPD competitors of Comcast can choose to use independent companies such as Viamedia so that they are not cooperating with a competitor for advertising sales.

After its acquisition of TWC, Comcast will have a greater degree of control in all aspects of the spot cable advertising market, including the NCC, Interconnects, and representation services. For example, in the New York DMA, the largest media market in the country, today there are two Interconnects, a "quasi-interconnect" managed by Cablevision that includes Comcast, and an Interconnect managed by TWC. Following the transaction, Comcast intends to integrate TWC's advertising operations with Comcast's. This increased control and leverage may give Comcast another lever to raise competing MVPDs' costs, restrict its competitors' advertising capabilities, and harm consumers.

Existing problems in the spot cable advertising market will be exacerbated post-acquisition. Comcast will move from partial control to a majority owner of NCC, the clearinghouse through which advertisers can purchase ads nationwide. By acquiring TWC, Comcast will own 80% of NCC and will likely acquire veto authority at the board level. This will give Comcast the ability to restrict its competitors' access to NCC. In addition to controlling two Interconnects in the New York DMA, Comcast will also gain increased control over the regional Interconnects. Post-acquisition, Comcast will control over 50% of all Interconnects in the United States and 18 of the top 25 Interconnects. This control will give Comcast another avenue through which it can harm competitors by giving it greater ability to refuse its competitors access to a broader range of Interconnects across the country.

<sup>73</sup> Application at 102, n. 257.

Furthermore, Comcast will gain additional control and leverage through its spot cable advertising representation services, which are already highly successful but will become even more so post-acquisition. With Comcast's increased control over NCC and the Interconnects, Comcast will have greater control in dictating whether competing MVPDs will be able to gain access to the NCC and the Interconnects, and the terms and conditions of such access. Comcast may force MVPDs to utilize its Comcast Spotlight for spot cable advertising representation as a condition for gaining access to the NCC and the Interconnects, in lieu of doing spot cable advertising on their own or through a competing spot advertising agent, like Viamedia.

Post-acquisition, Comcast will be in a stronger position to control the spot cable advertising market and disadvantage competing MVPDs. This may result in higher costs for competing MVPDs, small businesses and consumers who will lose the benefits of vigorous competition in this market.

- IV. THE ARBITRATION REMEDY THE COMMISSION HAS USED TO AMELIORATE COMPETITIVE HARMS OF OTHER TRANSACTIONS IS INADEQUATE TO PROTECT SMALLER MVPDS FROM THE HARMS OF THIS TRANSACTION
  - A. The Commission Created an Arbitration Remedy in Recognition of the Fact that its Rules Are Otherwise Insufficient to Protect Against Certain Merger-Specific Harms.

The Commission has long recognized that its program access rules, even in combination with voluntary commitments by merging parties, are inadequate to ameliorate the harms of transactions between programming suppliers and distributors.<sup>74</sup> In its most recent iteration in

<sup>&</sup>lt;sup>74</sup> See, e.g., *News Corp.-Hughes Order*, 19 FCC Rcd at 513-514, 551, ¶¶ 84-87, 169 (finding that a strategy of uniform price increases for video programming would not necessarily violate the program access rules and agreeing "with commenters that both the program access rules and the Applicants' proposed program access commitment are insufficient to protect against harms arising from News Corp.'s enhanced incentive and ability to use its market power in the market

Comcast-NBCU, the Commission once again imposed remedial conditions that employed a "baseball-style" arbitration process for programming disputes with Comcast, including those involving retransmission consent, with modifications over forms of this remedy the Commission had previously employed. In baseball-style arbitration, an aggrieved MVPD can initiate the process. Both the MVPD and Comcast are required to submit "final offers" at the outset to the arbitrator that each side believes reflects the fair market value of the programming at issue.<sup>75</sup> The arbitrator then chooses the final offer that most closely approximates the fair market value of the programming at issue. To determine fair market value, the arbitrator may consider any relevant evidence, including current or previous contracts between MVPDs and broadcast stations, national networks, or RSNs. Each party is also required to submit all other evidence that it intends to rely on in the arbitration.

Recognizing that small and mid-sized MVPDs could be at a particular risk, the Commission instituted one-way fee shifting in an attempt to make the arbitration remedy work for smaller MVPDs. Under the one-way fee shifting provisions, if an MVPD with 600,000 or fewer subscribers is the prevailing party in the arbitration, it is entitled to recover its legal fees and the costs of arbitration. Additionally, if the small MVPD loses, it is not required to reimburse Comcast's corresponding fees and costs.

for regional sports programming to the detriment of consumers."); Comcast-NBCU Order. 26 FCC Rcd at 4259, ¶ 49 (finding program access rules insufficient to remedy the potential harm of Comcast's increased incentive and ability to uniformly raise its rivals' fees).

<sup>&</sup>lt;sup>75</sup> The aggrieved MVPD is required to submit its final offer no later than the end of the 15th business day following its formal filing. Comcast is required to file its final offer within two business days of being notified that a formal demand for arbitration has been filed. See Comcast-NBCU Order, 26 FCC Rcd at 4365, Appendix B, ¶ 7.

Although ACA is deeply appreciative of the Commission's attempt to make the arbitration remedy useable for smaller MVPDs, the result can at best be described as an incomplete success. Unfortunately, for smaller MVPDs, in practice the *Comcast-NBCU* remedial conditions did not create a feasible remedy, leaving them unprotected from the recognized harms posed by the merger. These MVPDs will be at an even greater risk if the proposed transaction that will vastly expand Comcast's distribution footprint and programming heft is consummated. Indeed, the arbitration procedures were not designed for nor applied to address the scale of the harms described above.

The experience of ACA members before and after the Comcast-NBCU transaction has demonstrated the inadequacies of the Commission's baseball-style arbitration condition to address the harm from that transaction. In particular, the baseball-style arbitration provisions adopted in the Comcast-NBCU transaction are of no utility to smaller MVPDs due to the uncertainty and information imbalance in the arbitration process and the high fixed costs of arbitration, among other factors. Indeed, even when acting collectively through their buying group, the NCTC, smaller MVPDs were not adequately protected by the arbitral process. These factors are described in the sections below in additional detail.

Before proceeding to that detail, it bears emphasis that the other competition and policy threats from this transaction – disparity in bargaining power and control over spot advertising – aggravate the risk to small MVPDs from abuse by Comcast and TWC of their control over their owned content. That aggravated risk underscores the inadequacy of baseball-style arbitration.

B. Uncertainties in Preparing a Final Offer in Advance of Discovery Put Smaller MVPDS at Particular Risk in Initiating the Arbitration Process.

A number of uncertainties in preparing a final offer in accordance with the baseball-style arbitration process put small MVPDs at a competitive disadvantage when faced with an impasse in negotiations. These uncertainties amplify a small MVPD's hesitation to enter the arbitration process.

First, small MVPDs lack the critical information necessary to propose and predict a successful result. Because small MVPDs do not have precise information on the factors that an arbitrator would like use to make its determination on a fair rate, the MVPD is often unable to accurately and confidently estimate a fair rate. For example, small MVPDs do not have information on the existing and previous prices Comcast charges other similarly-situated MVPDs for the disputed programming. Nor do these small MVPDs know what other programmers are charging for similar programming. These programming rates may also include a "small MVPD premium," which increases the rate a small MVPD pays above a larger MVPD, based on their smaller amount of subscribers. While small MVPDs are generally aware of this "small MVPD premium," they are unable to accurately determine the amount of this premium. This is information that Comcast already has, and therefore, when Comcast is estimating a fair rate, it is more able to predict a successful result with significantly greater certainty.

As Mr. Fickle states, during NCTC's most recent renewal negotiations with Comcast at the end of 2012, NCTC considered utilizing the baseball-style arbitration condition the FCC imposed on Comcast when it acquired NBCU. NCTC had reason to believe that Comcast/NBCU was not offering it fair market rates, terms, and conditions. However, after careful consideration, NCTC decided that the arbitration condition was inadequate and ineffective, even with one-way fee shifting in the event it won, to address the unfair demands of Comcast/NBCU for several reasons, including NCTC's inability to reasonably evaluate the

likelihood of success in arbitration, "because [NCTC] lacked critical information on key factors that an arbitrator would likely use to make its determination of fair-market value. Without this information [NCTC] could not make an informed 'final offer.'"

Small MVPDs also do not have information on the costs of acquiring the content that comprises the programming at issue. While programmers, such as Comcast, generally have evidence of the value of the programming, including internal studies or discussions of the imputed value of the programming, small MVPDs who do not also distribute programming have no way of estimating these internal costs.<sup>77</sup>

In each stage of the arbitration process, from deciding to enter arbitration, to proposing a fair rate, this information imbalance puts small MVPDs at a distinct disadvantage in their ability to predict a successful result. This renders the arbitration process of no use to them.

Additionally, differences in arbitrators, and a lack of public information on similar arbitration decisions, also add to the uncertainty. This makes it almost impossible for a small MVPD to learn about the baseball-style arbitration process and to plan for the full time and effort of the process. ACA has anecdotal evidence of small MVPDs who have reported not understanding the general process or the steps required to go through the process. These MVPDs

Fickle Declaration, ¶¶ 11-12

<sup>77</sup> Fickle Declaration, ¶ 13 ("At the same time, Comcast/NBCU had perfect information. Comcast/NBCU possessed information on the prices it currently and formerly charged other MVPDs for its programming. It also knew the prices it granted to larger MVPDs as opposed to smaller MVPDs, and what other programmers charged for similar programming, particularly with regard to broadcast stations due to the fact that Comcast operated as an MVPD in dozens of designated market areas. We knew with all of this information available to them, they would be able to more accurately calculate a fair market value and provide it as its "final offer." Moreover, an arbitrator would find the information that Comcast had highly probative, and would likely rely upon it in determining which of the parties' 'final offer' is closer to fair market value.").

<sup>&</sup>lt;sup>76</sup> Fickle Declaration, ¶¶ 11-12.

admit that they underestimated the resources necessary to navigate the process and to predict a fair rate. Without access to similar arbitration decisions, the small MVPDs are often left with nothing to compare their rate estimates.

# C. Small MVPDs With Fewer Subscribers and Financial Resources are Risk Averse.

In addition to the uncertainty and information imbalance in the arbitration process, other risks add to the disadvantages inherent in the process for small MVPDs. For example, from the perspective of a small MVPD with fewer subscribers and financial resources, the high fixed costs of the arbitration process are generally in excess of any potential benefits. Arbitration involves drafting and submitting an initial filing, participating in multiple hearings and producing evidence of market rates. Each of these steps in the process requires assistance from attorneys and other consultants, including economists and data analysts, which adds to the costs. Even with one-way fee shifting, if the MVPD loses, these costs are not reimbursable. Additionally, the arbitration process, from start to finish, can take one year or longer to complete, and requires key personnel to take large amounts of time from their regular jobs, further adding to the costs.

The financial risk of arbitration for a buying group like the NCTC is not much better. As Mr. Fickle explains, his research revealed that "the average cost of baseball-style arbitration is approximately \$1 million. This represents a significant cost compared to both NCTC's annual operating budget, and our best guess at how much Comcast was charging us above the fair market value of the programming." As the end result, taking into account the risks posed by uncertainties as to timeframes and the lack of critical information to make an "informed 'final

<sup>&</sup>lt;sup>78</sup> Fickle Declaration, ¶ 14.

offer," NCTC found the risks and costs of baseball-style arbitration would outweigh any potential benefits obtainable through a successful arbitration.<sup>79</sup>

When all of the costs of the arbitration process are added together, this amounts to a relatively large share of a small MVPD's revenues, especially as compared to the average number of subscribers. The costs of proceeding through the arbitration process are relatively fixed regardless of an MVPD's number of subscribers. However, the potential benefit arising from the arbitration – lower programming fees – is directly proportional to the number of subscribers. Therefore, the cost of engaging in an arbitration proceeding becomes progressively less attractive to an MVPD the smaller it is. The Commission recognized this reality in the *Comcast-NBCU Order*: "Given the size of their subscriber bases and financial resources, small and medium-sized MVPDs may be less able to bear the costs of commercial arbitration than large MVPDs, thus rendering the remedy of less value to them."

Additionally, the MVPD risks losing the arbitration and bearing the total costs of the arbitration and the added burden of higher programming costs. With this end result, the small MVPD has expended hundreds of thousands of dollars and endless hours to go through the arbitration, only to then pay higher rates for programming. Professor Biglaiser analyzes these risks and costs in the accompanying analysis.<sup>81</sup> These possibilities provide a risk-averse small MVPD the incentive to save the time and effort required to go through the process, and to accede to the pressure and demands of the programmer.

<sup>79</sup> Fickle Declaration, ¶ 15.

<sup>80</sup> Comcast-NBCU Order, 26 FCC Rcd at 4262, ¶ 58.

<sup>81</sup> Biglaiser at 33-36.

#### D. Smaller MVPDs are at Greater Risk of Retaliation by Comcast.

ACA believes that the risk of retaliation is an additional reason that arbitration is an inadequate remedy for small and mid-size MVPDs. ACA has heard anecdotal evidence from MVPDs who feel that programmers have an incentive to make up any expenses from the arbitration and any lost fees as a result of a lost arbitration through future contract negotiations. These MVPDs feel that using arbitration is a "zero sum game," especially when the next time they need to negotiate the arbitration conditions have expired, or are no longer available to them. In such a case, the lack of availability of arbitration for the next negotiation is a deterrent for using the arbitration in the first instance.

# E. Other Factors Add to the Problems with Use of the Arbitration Remedy by Smaller MVPDs.

In addition, other factors exacerbate problems with the arbitration remedy. Smaller MVPDs experience problems getting started in the process. When conditions are first introduced and there is no track record of arbitration results to consult, small MVPDs will be especially poorly informed and skeptical of the process. The first few MVPDs who test the remedy will bear especially high risks. Accordingly, there is a particular risk that arbitration will never be tested because of this higher test risk. This continues to be a problem with regard to the conditions adopted to mitigate the harms of the Comcast-NBCU transaction, which for many of the reasons addressed herein have never been utilized by any small MVPDs.

Another problem is that a vertically integrated programmer subject to an arbitration provision, like Comcast, is likely to outspend its opponents in arbitration. Comcast may find it both rational and profit-maximizing to outspend its opponents in the arbitration process. The programmer will have a reputational incentive to expend significant effort in its earliest

arbitrations, particularly with risk-averse small MVPDs, to discourage other small MVPDs from undertaking subsequent arbitrations. Moreover, since a vertically integrated programmer like Comcast will be in multiple arbitrations and can reuse many aspects of its preparations in later arbitrations, it will likely be able to do more with the money it spends.

#### V. CONCLUSION

The Applicants propose an unprecedented consolidation of content and expansion of distribution. The proposed transaction would create significant horizontal and vertical harms, resulting in higher costs to consumers and reduced competition, especially with the smallest MVPDs. Without adequate remedies, consumers and competition will suffer from the Comcast-TWC-Charter deal. Should the Applicants be unable to develop and propose enforceable commitments to address the harms identified by ACA, the Commission must do so to protect competition and consumers.

Respectfully submitted,

#### AMERICAN CABLE ASSOCIATION

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## EXHIBIT A

## The Harms of Comcast-TWC-Transaction\*

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August 25, 2014

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#### I. Introduction

The proposed transactions among Comcast, Time Warner Cable (TWC), and Charter

Communications (Charter) will exacerbate the competitive harms that resulted from the earlier merger
of Comcast and NBC Universal (Comcast-NBCU) distribution and programming assets. In my view,
rival multichannel video programming distributors (MVPDs), and their subscribers, will pay higher
fees for Comcast-affiliated programming as a direct result of the Comcast-TWC-Charter transactions
due to Comcast's increased vertical control of important programming assets and its increased overlap
with multichannel video programming distributors ("MVPDs") within the industry. Furthermore, by
combining the nation's two largest cable operators and increasing the combined entity's share of
MVPD subscribers, Comcast-TWC will have an increased incentive to disadvantage its rivals due to
enhanced bargaining power in the programming market. Lastly, I argue the increased competitive
harm that results from increased vertical integration requires the Federal Communications Commission
(FCC) to adopt stronger remedies than the conditions imposed on Comcast in the Comcast/NBCU
Order. The existing conditions suffer from flaws that make them inadequate to address the increased
harm.

My analysis is as follows. In Section II, I describe the proposed transactions. I then discuss the vertical harms resulting from the proposed transactions in Section III, where I discuss how the proposed Comcast-TWC-Charter transactions merger increase the vertical harms caused by the Comcast-NBCU merger. In Section IV, I analyze the horizontal aspects of the Comcast-TWC-Charter transactions. I argue that the increased bargaining power Comcast will acquire will result in harm to other MVPDs and their subscribers. I follow the analysis of harms in Section V with an analysis of how the commercial "final offer" arbitration process used by the FCC to ameliorate the competitive

harms of the Comcast-NBCU merger has flaws that make the process ineffective at addressing the competitive harm, particularly for smaller MVPDs.

## II. Description of Transactions

The Comcast-Time Warner Cable-Charter deal involves actors that have significant presence in both the (downstream) MVPD industry, which distributes video programming to consumers, and the (upstream) video programming industry, which provides this programming to these distributors.

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<sup>&</sup>lt;sup>1</sup> ACA has provided this estimate of residential homes passed and other the estimates used throughout this paper. ACA calculated this number using the lists of census blocks provided by the Applicants (based on their December 2013 National Broadband Map data) in their July 31, 2014 letter, which indicates where the companies make their broadband service available. Using census data, ACA totaled the number of housing units in each census block deemed served by the Applicants. ACA believes, and I agree, that the Applicants' broadband service territory is a good proxy for their video service availability. Due to the fact that applicants might not make video service available to all locations in a census block, these numbers might slightly overstate actual homes passed by the applicants for all services offered by the applicants, but ACA believes despite this fact, the best means of estimating residential video homes passed is to rely on this data which is the most granular available. In this paper, I use the term "homes" passed. My use of "homes" refers to housing units in a census block.

systems in four states serving approximately 212,000 residential subscribers. Midcontinent has a legal right to obtaining programming under Comcast's programming agreements.<sup>2</sup>

<sup>&</sup>lt;sup>2</sup> Applications of Comcast Corp. and Time Warner Cable, Inc. for Consent to Assign or Transfer Control of Licenses and Authorizations, MB Docket No. 14-57, Comcast letter dated June 25, 2014, at 12, n.30.

<sup>&</sup>lt;sup>4</sup> While TWC does not own BHN or make its managerial decisions, TWC and subsequently Comcast once the transactions are consummated, does sell operational services to BHN and [[

programmers Discovery Communications and Starz, the Discovery Communications and Starz networks are considered attributable to Charter pursuant to the Commission's attribution rules.<sup>5</sup>

Popular networks deemed attributable to Charter under FCC rules include Discovery Channel, TLC, Animal Planet, The Oprah Winfrey Network, and Starz.

In the two proposed interrelated transactions, Comcast will acquire 100 percent of TWC's equity and its 11.4 million customers. Comcast will then divest TWC systems serving approximately 1.5 million existing subscribers directly to Charter; (2) Comcast and Charter will transfer assets, respectively serving approximately 1.5 million existing TWC customers and 1.6 million Charter customers, thereby enhancing the geographic clustering of both companies; and (3) Comcast will form and spin off to its shareholders a new, independent, publicly-traded company ("SpinCo") that will operate systems serving approximately 2.5 million existing Comcast customers. Charter will acquire a one-third interest in SpinCo's equity, and enter into a services agreement with it.<sup>6</sup>

<sup>&</sup>lt;sup>5</sup> Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Fifteenth Report, MB Docket No. 12-203 (rel. Jul. 22, 2013), Appendix B, National Programming Services, Table B-1 (listing Liberty Media-affiliated programming networks)

<sup>&</sup>lt;sup>6</sup> Under the agreement, SpinCo has the right to have Charter purchase programming on its behalf.

homes at its start, and serve 2.4 million residential customers. Comcast will acquire all programming assets of TWC.

In addition, Comcast will acquire TWC's legal interest in TWE-A/N and in the licenses and authorizations held by BHN. Comcast offers no evidence that it will not assume the same existing contractual arrangement with BHN that TWC currently has with BHN.

I will demonstrate that, by increasing Comcast's total number of homes passed through the acquisition of TWC and Charter systems and adding the TWC programming to Comcast's already prodigious suite of programming assets, the transactions will adversely affect a majority of the MVPD subscribers served by *other* distributors. It will also harm customers of Comcast, as Comcast will have incentive to increase the prices it charges to its own video customers.

### III. Vertical Harms of the Comcast-TWC-Charter Transaction

As the Commission found in Comcast-NBCU merger review, the combination of Comcast distribution assets and NBCU programming assets gives Comcast an incentive and ability to charge other MVPDs higher prices for its programming. As a result of the current transaction, this existing vertical harm will grow larger because the merger increases the opportunity cost to Comcast from selling programming. There are two ways in which the opportunity cost increases. The first is the increased opportunity of attracting subscribers from rival MVPDs due to the increased number of homes passed by Comcast as a result of its cable system acquisitions. The second is the increased profits of attracting new subscribers due to the greater margins resulting from the merger. The higher opportunity cost for selling its programming due to the merger gives Comcast a greater incentive to

raise the price of its programming to rival MVPDs. These MVPDs will pass the increase in programming cost, in part or whole, through to their subscribers.

Another vertical harm that was not considered, but should have been, in the Comcast-NBCU review is the price effect that has Comcast and then subsequently rival MVPDs raising their prices due to the acquisition by Comcast of NBCU programming assets. I will examine this harm. Finally, I note the transaction is expected to increase Comcast's profits per subscriber due to the increased bargaining power that Comcast will gain when it buys programming for its larger volume of subscribers, and how this will harm the subscribers of MVPDs buying Comcast's programming.

I begin by describing the bargaining framework that demonstrates the increased opportunity cost Comcast has in selling its national cable programming networks, NBC O&O stations, and RSNs to other MVPDs. To demonstrate that there will be an overall increase in the vertical harm as a result of this deal, I analyze two categories of firms that would likely face a vertical harm due to the merger in the relevant market for each programming asset. The first is large MVPDs that currently have substantial overlap with Comcast and generally negotiate programming deals on their own. The second are smaller MVPDs, which generally obtain their programming through the National Cable Television Cooperative (NCTC)<sup>7</sup>. Relying on homes-passed data for the applicants and other MVPDs, I show that both categories of firms will face more head-to-head competition with Comcast in the relevant distribution markets if the merger is approved.

A. Bargaining Framework to Analyze Vertical Harms.

<sup>&</sup>lt;sup>7</sup> The NCTC acts as a bargaining agent for more than 900 small and medium-sized cable operators.

To analyze the vertical harms of the Comcast-TWC merger, I will use the bargaining framework adopted by the FCC for the Comcast-NBCU merger in its analysis of the merger's competitive harms. I will use the Comcast-NBCU framework to demonstrate the two classes of vertical harms that arise from the merger due to Comcast's increased opportunity cost of selling programs to rival MVPDs. The first vertical harm arises from Comcast increasing the number of homes it passes because it will be in a better position to attract subscribers from rival MVPDs. The second vertical harm arises from either increasing the profitability of its video service as a result of efficiencies Comcast creates from the merger and/or its increased bargaining leverage over vendors of inputs to its business. I analyze each of these harms in turn using the framework adopted by the FCC in the Comcast-NBCU merger.

The bargaining framework computes the opportunity cost that Comcast incurs by selling programming to a rival. A higher opportunity cost for providing programming to a rival provides an incentive for Comcast to raise its price for that programming. This increased cost to rival MVPDs will be passed on, in whole or in part, on to the rival MVPD's subscribers in terms of higher cable fees.

The opportunity cost for Comcast to sell its programming assets to a rival MVPD, C, is equal to

$$C = \alpha d\pi$$

In this formula,  $\pi$  is Comcast's monthly profit if it attracts the consumer away from a rival MVPD. The probability that a given consumer leaves the rival provider, d, is referred to as the diversion rate.

<sup>&</sup>lt;sup>8</sup> Applications of Comcast Corp., General Electric Co. and NBC Universal, Inc. for Consent to Assign Licenses and Transfer Control of Licensees, MB Docket No. 10-56, Memorandum Opinion and Order, 26 FCC Rcd 4238, 4247, ¶ 46 & Appendix B, Technical Appendix, Section I.B. (2011) ("Comcast-NBCU Order").

The share of subscribers that leave the rival MVPD due to a price increase that will go to Comcast instead of another rival MVPD provider is  $\alpha$ .

As in the FCC adopted framework for the Comcast-NBCU merger, I assume the profit derived from obtaining a customer from a rival does not depend on which rival it comes from and that the diversion rate does not change due to the Comcast-TWC-Charter transaction if Comcast's programming price increases or if it is withheld from a competitor MVPD.

I assume, following the Nash Bargaining Solution as adopted by the FCC in the Comcast-NBCU mergers that each dollar increase in the opportunity cost will result in a 50-cent increase in the cost of programming. That is, Comcast captures one half the gains from the increase in opportunity cost when negotiating with an MVPD. Thus, each calculation will only differ by  $\alpha$ , the proportion of consumers that go to Comcast. The design of the framework allows us to examine the additional opportunity cost that Comcast has due to the merger, which will show up only due to how  $\alpha$ , which is a measure of Comcast's market share and represents the possibility that a consumer could switch to Comcast, changes due to the merger.

#### B. Framework for Determination of $\alpha$ .

In the Comcast-NBCU transaction, the Commission recognized the harm created by the vertical integration of Comcast's distribution assets with NBCU's programming assets. <sup>10</sup> In this paper, one goal is to show there is an increased incremental harm due to the transaction. By focusing on the increased incremental harm, it's acceptable to generalize the framework that the FCC adopted for the

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<sup>&</sup>lt;sup>9</sup> Comcast-NBCU Order 26 FCC Rcd at 4247, Appendix B, Technical Appendix, Section I.B.

<sup>&</sup>lt;sup>10</sup> *Comcast-NBCU Order*, 26 FCC Rcd at 4252 − 4259, ¶¶ 34-48.

Comcast-NBCU for determining  $\alpha s$  because simply showing an increase in incremental harm is not sensitive to the modeling assumptions made by how subscribers distribute themselves across firms when they leave a rival MVPD.

My analysis is based on the standard discrete choice model. <sup>11</sup> When consumers are facing a decision about what product to purchase, they evaluate the intrinsic qualities of the products and the price of each product in their feasible set of choices. They then choose the product attribute/price combination that maximizes their utilities. A product's quality has features where all consumers may agree about the product's quality, such as the reliability of the product, and features where consumers may have different rankings for the product's quality, such as the program offering. The first types of features are known as vertical features, while the second are known as horizontal or idiosyncratic features. They also may have different willingness's to pay for higher qualities of a particular feature. The differences in consumers' willingness to pay for features and the idiosyncratic preference differences are the reasons that not all consumers will go to the same MVPD.

When consumers are making their decision about which MVPD to subscribe to, they evaluate the offerings' vertical and horizontal features or qualities and the prices for each service. An MVPD will have a larger market share than an MVPD that offers a lower value for a large number of consumers.

To demonstrate, define Comcast's market share in a particular market, including the national market, as  $s_c$ . The market share of a rival MVPD that Comcast is selling one of its sets of programs is defined as  $s_r$ . The remaining 1- $s_r$ - $s_c$  are the markets shares of all the other MVPDs in the relevant

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<sup>&</sup>lt;sup>11</sup> See Anderson, de Palma, and Thisse, Discreet Choice Theory of Product Differentiation, 1992 MIT Press.

market. Let  $\theta$  be the proportion of a rival MVPDs' consumers who could switch to Comcast if a rival raised its prices.

The  $\alpha$  for Comcast for a particular market is

$$\alpha = f(s_{c}, 1-s_{c}-s_{r}, \theta)$$

To interpret this formula, I assume that Comcast and all other firms' market shares are positively related to the value rankings. Furthermore, these value rankings do not change when the Comcast-TWC-Charter transaction is consummated. Thus, as consumers leave a rival MVPD due to a price increase from Comcast, they are more likely to subscribe to Comcast the larger Comcast's market share is. Likewise, they are less likely to go to Comcast, the larger the market shares of all other MVPDs that are not Comcast. That is,  $\alpha$  is increasing in the first argument and decreasing in the second argument. Finally, I assume that the larger the proportion a rival MVPD overlaps with Comcast, the higher probability that a subscriber who leaves the rival will go to Comcast. That is,  $\alpha$  is increasing in its third argument. These are the only assumptions that I make on  $\alpha$ . They are very mild and intuitive assumptions and thus the sign of the harm due to the transaction that I find is quite robust to the modeling assumptions.

The key to the first class of vertical harms is that as consumers leave an MVPD due to the withholding of programming or higher prices, they will go to another MVPD as an increasing function of Comcast's market share, which is a proxy of its value to consumers. This harm will increase by demonstrating that the transactions takes place, the change in overlap between Comcast and a rival MVPDs will rise.

C. Determination of Incremental Vertical Harm due to the Merger

To compute the additional vertical harm due to the merger, one would need to compute for each class of rival, large and small, and for each possible programming category: NBC national cable programming suite, retransmission rights for O&O stations, and RSNs.

The incremental increase in harm for Comcast to sell programming to a rival MVPD is

$$H = \pi dN(\alpha_M - \alpha_N)/2 \tag{1}$$

This harm has several aspects. The monthly profit per subscriber is  $\pi$ . The number of subscribers that a rival MVPD has is N. The diversion rate is d. The 2 represents half of the increased opportunity cost that will be passed on as a higher cost to the MVPD and that this cost increase is then passed on to consumers. In determining the harm before and after the merger, I assume the diversion rate of the programming Comcast owns and acquires is the same as before the merger. I also assume that the profits per subscriber of the systems being acquired are relatively similar as those of Comcast. Accordingly, the incremental harm boils down to how many more subscribers are now potential customers for Comcast compared with the pre-merger situation. This is represented by Comcast's  $\alpha$  going from a pre-merger situation of  $\alpha$ <sub>N</sub> to a post-merger and  $\alpha$ <sub>M</sub>.

D. Analysis of the Overall Increase in Vertical Harms

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<sup>&</sup>lt;sup>12</sup> Later I mention that Comcast is acquiring TWC's regional sports networks in New York and Los Angeles, and that the diversion ratio in these markets might increase to the extent that Comcast threatens an MVPD with simultaneously pulling its existing programming and the TWC's RSN.

<sup>&</sup>lt;sup>13</sup> I reviewed data from a respected Wall Street analyst that showed the estimated video gross profit dollars per subscriber for Charter and Comcast to be \$37. The estimate for Time Warner Cable was \$34. Even though the average profits of TWC subscribers are not quite as high as those for Comcast's current subscribers, it is safe to assume that TWC's profits would trend toward being similar to Comcast within a very short time. This is part of the alleged efficiencies that Comcast is bringing to these subscribers.

In the following, I examine the two groups of firms that will be impacted by Comcast's increased incentive and ability to charge higher prices for its programming as a result of its increase in homes passed. The first group includes large MVPDs that currently have substantial overlap with Comcast and generally negotiate programming deals on their own. These MVPDs include the two direct broadcast satellite providers (Dish and DirectTV), and the two largest telcos providing video service (AT&T and Verizon.) The second group includes more than 900 small and medium-sized MVPDs that generally buy a substantial share of their programming through the National Cable Television Cooperative (NCTC). This group includes MVPDs currently competing head-to-head with Comcast, TWC, and Charter. Some of these MVPDs will compete either more or less against the applicants if the transaction is approved, and some will compete at the same level because the systems they compete against are not changing hands as part of the deal. This second group of small and medium-sized MVPDs also includes those that do not compete directly against Comcast, TWC, or Charter before the transaction and will not compete directly against Comcast, Charter, or SpinCo after the transaction. Given that Comcast negotiates a single master agreement with NCTC and it generally expects all but NCTC's largest members to opt into the agreement, to the extent that Comcast has an incentive to charge higher prices to one or more of its members, Comcast will charge these higher prices to NCTC. This means that operators who do not compete directly with Comcast, but opt-in to NCTC's master agreements, will also be harmed.

Not included in these categories are large MVPDs that generally negotiate programming deals on their own, but who do not currently have significant competitive overlap with the applicants. With respect to negotiating for Comcast programming, these operators include: Charter (including SpinCo), Cox, Cablevision, BHN, and Midcontinent. With respect to Charter programming, these operators will include: Comcast, Cox, Cablevision, and BHN, and Midcontinent.

There are four main classes of programming assets that Comcast owns or will own after the merger that need to be assessed: (1) the suite of national cable programming networks owned by Comcast; (2) the NBC Network O&Os in ten designated market areas (DMAs); (3) the RSNs that Comcast owns; and (4) the two RSNs that TWC currently owns that will pass to Comcast. My report focuses on the harms caused to MVPDs that carry the first two categories of programming.<sup>14</sup>

#### E. Vertical Harms Involving Large MVPDs that Compete with Comcast

I first take up the harms from the merger for MVPDs that currently have large competitive overlaps with Comcast and generally obtain their programming from programmers through direct deals. This group includes: DirectTV, Dish, Verizon, and AT&T. In the following, I examine whether there is a competitive increase for Comcast's national cable programming networks and its O&O markets.

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<sup>&</sup>lt;sup>14</sup> With regard to Comcast's nine RSNs, the precise footprint of the RSNs is not publicly available, making an analysis of the impact difficult to quantify or reach qualitative conclusions. Therefore, I do not include this analysis in my report. I would encourage the Commission to request from Comcast the census blocks in which its regional sports networks are made available to MVPDs, and amount of sports programming available to be offered by an MVPD from the RSN in each census block, in order for the data to be subsequently available to commenters to make more certain determinations on this issue.

<sup>&</sup>lt;sup>15</sup> Data for the number of housing units in 2013 comes from SNL Kagan, U.S. Multichannel Industry Benchmarks, <a href="http://www.snl.com/interactivex/MultichannelIndustryBenchmarks.aspx?startYear=2013&endYear=2014">http://www.snl.com/interactivex/MultichannelIndustryBenchmarks.aspx?startYear=2013&endYear=2014</a> (visited August 19, 2014). This number is equal to the total number of housing units in all census blocks in all 210 designated market areas, the non-designated market areas of Alaska, and Puerto Rico.

competitive overlap with Comcast will increase about {{ }} from {{ }} to {{

As a result of Comcast's acquisition of TWC's interest in TWE-A/N, Comcast will also have an incentive and ability to charge DISH and DirecTV higher prices in markets where the DBS providers compete against BHN. BHN matters to Comcast's profits in via two different ways. First, TWC – which will be united with Comcast after the transactions are completed – provides services to BHN. As BHN becomes more profitable, Comcast will be able to raise the price for these services because their value to BHN will increase. This effect arises from various bargaining models including the Nash Bargaining Solution. Second, [[ ,]] the more subscribers that Comcast has to offer programmers the more bargaining power and hence lower price it can obtain. [[ given Comcast's historic ability to obtain the lowest prices in the industry for programming. When Comcast negotiates with programmers, programmers will realize that BHN will not negotiate with them separately, and that failure to reach an agreement with Comcast will mean the loss of access to not only Comcast's customers, but also to BHN's customers. Therefore the more customers served by BHN, the more bargaining power that Comcast will have in its negotiations. Given Comcast's interest in preserving BHN's customers, Comcast will have an incentive and ability

to charge higher prices to BHN's MVPD rivals. BHN currently passes approximately 4.1 million

homes. 16 Taking into account BHN's competitive overlap with the two DBS providers, which accounts for about 3% of the DBS providers' footprint, these DBS providers' competitive overlap with Comcast combined with their competitive overlap with BHN amounts to a total increase in competitive overlap of {{ }} for each company. 17

There is also an increase in Comcast's opportunity costs regarding retransmission consent for the NBC O&O stations. None of the spinoffs to Charter and SpinCo come from any of DMAs served by the NBC O&O stations. However, in four of the markets – Dallas, Los Angeles, New York, and San Francisco – Comcast will have a larger presence due to its acquisition of TWC (Los Angeles and New York) and its swap of systems with Charter (Dallas and San Francisco). According to data }} to {{ } due to an increase in Comcast's homes passed in these markets. Thus, Comcast will have an incentive to raise its retransmission consent prices in these four markets to the national MVPDs, which will result in higher prices for the subscribers of these MVPDs, because part, if not all, of the increase in cost will be passed onto the subscribers.

For Verizon's FiOS service, <sup>18</sup> the competitive overlap with Comcast will {{ following markets: New York, Los Angeles, Dallas, Buffalo, Syracuse, Albany, and Palm Springs. Verizon also competes against BHN in the Tampa-St. Petersburg (Sarasota), FL market. BHN's

<sup>&</sup>lt;sup>16</sup> This number is derived based on Bright House Networks reporting of housing units passed on the National Broadband

<sup>&</sup>lt;sup>17</sup> I recognize that a customer coming to BHN from a rival MVPD is different than if it went to Comcast. I also acknowledge that getting subscriber is more profitable for it than if the subscriber went to BHN. My view is that while the profit is not as high for such a subscriber it is still positive and raises the opportunity cost for Comcast to selling programming to BHN's rival MVPDs.

18 To determine Verizon FiOS's homes passed, ACA relied on the company's homes passed data submitted to the National

Broadband Map for its FTTH service.

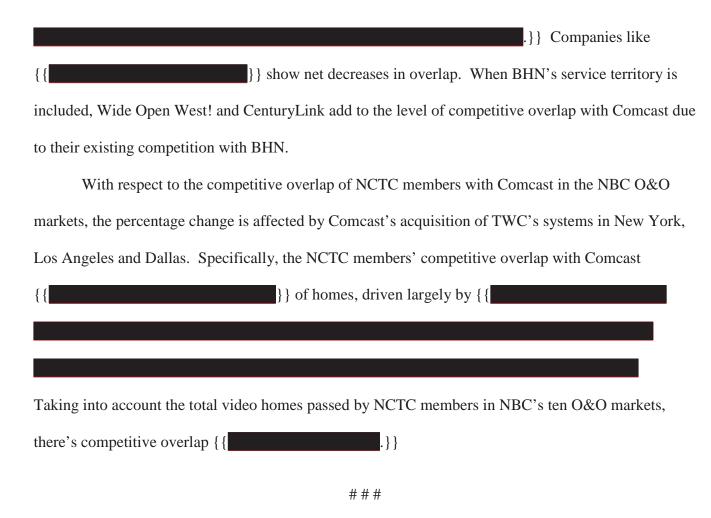
footprint overlaps with 7% of Verizon's. Totaling the change in Verizon's competitive overlap with Comcast and the competitive overlap with BHN results in an overall {{

Due to an inability to determine with precision the video footprint of AT&T's U-verse service, I am omitting them from this analysis, but return later to discuss that a conclusion can be reached about the overall harm of the Comcast-TWC-Charter deal to the MVPD industry and its customers as a result of Comcast's vertical integration and increased competitive overlap.

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<sup>&</sup>lt;sup>19</sup> Midcontinent Communications is a member of NCTC, but due to its right to opt into Comcast's programming deals, they too have been excluded.

<sup>&</sup>lt;sup>20</sup> See footnote 17.



Although precise information on all MVPDs is not available, I feel confident reaching the conclusion that the Comcast-TWC-Charter deal will result in an overall increase in vertical harm to consumers based solely on the change in competitive overlap between Comcast and the rival MVPDs for which I have data.<sup>21</sup> I reach this conclusion by taking account of the fact that MVPDs serve

reliable data for AT&T. Given these results, I believe consumers overall will likely be harmed by the Comcast-TWC-

approximately 100 million customers. Excluding the customers of Comcast (29.1M subs), BHN (2.1M subs) and MidContinent (0.2M subs), who will not be harmed by Comcast's increased vertical integration, if the deal is approved the universe of subscribers served by other MVPDs and potentially harmed decreases to 68.6 million households. Of these 68.6 million households, some are served by large MVPDs who generally obtain their programming from programmers through direct deals but do not substantially compete with Comcast now, and will not if the deal is approved. Subscribers to these MVPDs are unlikely to see an increase or decrease in harm if the Comcast-TWC-Charter deal is approved. These are: Charter (5.6M subs), Cox (3.2M subs), Cablevision (2.8M subs), and SpinCo (2.4M subs). In total, these MVPDs will account for 14 million subscribers. This leaves MVPDs serving approximately 54.6 million subscribers that may be harmed by the Comcast-TWC-Charter deal. As Table 1 below shows, of these 54.6 million subscribers, 34.3 million (62%) are served by the two DBS providers, who will see an increase in their competitive overlap with Comcast due to Comcast's acquiring more systems, and who will see higher prices for their customers. Verizon, who three operators serving 39.7 million households (representing 72% of all subscribers served by operators potentially affected by the Comcast-TWC-Charter deal) {{ considering smaller cable operators that generally negotiate direct deals in the aggregate, there is { }}. In total, these operators serve approximately 9 million subscribers. Thus, among MVPDs serving 54.6 million subscribers, those serving 49.2 million subscribers (representing 90% of all subscribers served by operators potentially affected by the deal) .}} As discussed, due to a lack of data on AT&T U-verse, it is not possible to

Charter deal as a result of the increased homes passed of Charter and SpinCo and its competitive impact on MVPDs who serve a majority of customers whose MVPDs are affected by the vertical harm.

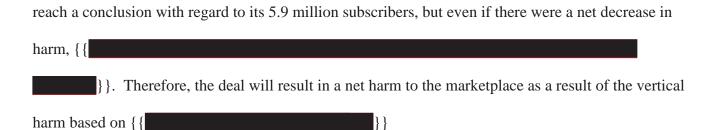


Table 1.

MVPDs	Subs	Pre Merger Competitive Overlap with Comcast	Post Merger Competitive Overlap with Comcast	Difference	Competitive Overlap with BHN	Total Difference
DIRECTV	20.2M	{{	{{		3%	
DISH	14.1M	{{	{{		3%	
Network						
NCTC	9.0M	{{	{{		4%	
Verizon	5.4M	{{	{{ }}}		7%	
AT&T	5.9M	N/A	N/A	N/A	N/A	N/A

#### G. Vertical Harm: The Price Effect for Comcast Subscribers

In the FCC's analysis of the vertical harm of the Comcast-NBCU merger, it found that Comcast would have an incentive to charge higher prices to rival MVPDs for the newly acquired NBCU programming than NBCU had alone due to Comcast's higher opportunity cost for selling the programming to its rivals. The analysis did not take account of another set of vertical harms arising from the merger. These harms stemmed from Comcast's incentive to raise prices to its own subscribers due to its acquisition of NBCU programming. Before the merger, if Comcast raised the price to its subscribers and then lost some of them, it would make no profits at all on the lost subscribers. Once Comcast acquired the NBCU programming, if it raises its price to subscribers and some of them leave for other MVPDs, Comcast will still make some profits from these lost subscribers

by selling its programming to the other MVPDs. This effect will increase Comcast's incentive to raise its own subscription price, and is in addition to the increased opportunity cost effect previously identified with respect to the Comcast-NBCU merger. With this higher opportunity cost, Comcast will charge more for the programming to its subscribers, but will experience less loss in profit due to subscriber defections. Thus, not only were Comcast's rivals hurt by the merger with NBCU, but Comcast's own subscribers were hurt.

To see this effect algebraically, we can write Comcast's profits as

$$\pi = p^{c}\alpha_{c}\big(p^{c},p^{R}(\omega^{c})\big) + \omega^{c}\alpha_{R}(p^{c},p^{R}(\omega^{c}))$$

The first terms are the profits that Comcast gets from its own subscribers. It is the price that Comcast charges them,  $p^C$ , times Comcast's market share  $\alpha_C$ , which is a function of Comcast's subscription price and the subscription of the rival  $p^R$ . This subscription price is a positive increasing function of the price that Comcast charges for its programming,  $\omega^C$ . The second set of terms is the profits that Comcast obtains from selling its programming to the rival. It is the price of the programming times the rival's market share. An increase in Comcast's subscription price  $\Delta p^C$  results in a change in profits of

$$\Delta \pi = \Delta p^{\mathrm{C}} * \alpha_{\mathrm{C}} (p^{\mathrm{C}}, p^{\mathrm{R}}(\omega^{\mathrm{C}})) + p^{\mathrm{C}} * \Delta \alpha_{\mathrm{C}} / \Delta p^{\mathrm{C}} * \Delta p^{\mathrm{C}} + \omega^{\mathrm{C}} * \Delta \alpha_{\mathrm{R}} / \Delta p^{\mathrm{C}}$$

If Comcast did not have programming to sell to its rival, then the first two terms of the change in profits represent the standard trade-off that a firm faces when contemplating a price rise: the increase in revenue from the consumers that continue to subscribe vs. the loss in subscribers due to the price increase. At the margin, Comcast would just balance these two. The third term represents the increase in Comcast profit by the rival's market share growth due to Comcast's price increase times the

price that Comcast charges to its rival for its programming. As Comcast raises its subscription price, this increases the rival's market share. This added effect induces Comcast to charge a higher price to its subscribers than if it did not have programming.

Furthermore, this additional Comcast subscriber price effect generates an additional harm to the subscribers of the rival MVPDs subscribers. In almost all standard oligopoly pricing models, if one competitor raises its price, its rivals will raise their prices due to the reduced outside options of its current customers. That is, when a firm raises its price, this softens price competition among the rival firms. In economic terms, the firms' prices are known as strategic compliments and their best response to a higher price by a competitor is to increase their price.<sup>22</sup>

Although this harm was not identified in the Comcast/NBCU merger review, it occurred and has existed since that merger was approved. Of relevance to the pending transaction is the fact that Comcast's incentive to raise its rivals costs is now increasing due to Comcast/TWC, and that these pricing effects on Comcast customers will further increase as a result of the merger.

#### H. Increase in Profits Per Subscriber and Higher Opportunity Costs

I discuss now how the alleged efficiencies that Comcast claims for the merger will raise its opportunity cost of providing programming to rival MVPDs. In the previous discussion, I assumed that Comcast's profit per subscriber for the systems it is acquiring would be the same as Comcast's profits per subscriber for its existing systems. Next, I argue that Comcast's profits per subscriber for its existing systems are likely to increase due to the deal, and this will increase its incentive to extract

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<sup>&</sup>lt;sup>22</sup> See <u>Multimarket Oligopoly: Strategic Substitutes and Complements</u>.by Jeremy Bulow, John Geanakoplos and Paul Klemperer, *Journal of Political Economy*, 1985, Vol. 93, 488-511.

higher prices from rivals to the systems where it's acquiring, and from rivals of its existing systems that remain within Comcast's control.

I. Efficiencies Gained by Comcast and Increased Incentives to Raise Program Prices

First, I address the incentive to raise programming prices due to the "efficiencies" that Comcast claims. In its FCC filings, Comcast claims that there are large benefits to consumers due to increased efficiencies from the merger. Rosston and Toppler state that:<sup>23</sup>

To the extent that the firm earns positive cash flows from each additional customer, a greater scale will result in a larger stream of positive cash flows. Comcast uses the net present value framework in helping to evaluate business decisions.

Thus, the alleged efficiencies due to the merger will result in higher profit per Comcast subscriber. This will increase the opportunity cost to Comcast of providing programming to rival MVPDs in areas where it is acquiring systems and where its current systems exist and thus increase the cost of such programs.

Rosston and Toppler describe the possible efficiencies for the X1 technology and for video on demand (VOD).<sup>24</sup> Both of these alleged efficiencies, to the extent they exist, will lead to higher profits per subscriber for all of Comcast subscribers due to increased demand for Comcast's services and more use of video on demand (VOD). The result of higher profitability per subscriber will increase Comcast's opportunity cost of selling its programming to competitors, which will lead to higher prices for competitors to buy Comcast's programming. Rosston and Toppler do not supply any specific cost

<sup>24</sup> Gregory L. Rosston and Michael D. Topper, "An Economic Analysis of the Proposed Comcast – Time Warner Cable Transaction" ¶88 and 106 (April, 2014).

<sup>&</sup>lt;sup>23</sup> Gregory L. Rosston and Michael D. Topper, "An Economic Analysis of the Proposed Comcast – Time Warner Cable Transaction" ¶ 46 (April, 2014).

estimates for the potential efficiencies. While this makes putting a number on the additional increase in opportunity cost for Comcast difficult, it should be clear that the larger Comcast's claimed efficiencies the larger the incentive to raise its programs' prices. In the next section discussing the horizontal harms of the merger, I describe another factor increasing Comcast's opportunity cost that is a result of Comcast increasing its bargaining leverage with other programmers through the addition of subscribers coming from TWC and Charter. This will allow Comcast to obtain lower programming prices, and better terms and conditions. Whether due to efficiencies or some other explanation, by lowering its programming costs, Comcast will be increasing its profitability per subscriber and increasing its opportunity cost in selling its programming to rivals.

## J. Diversion Rate Changes Due to the Merger

Similar to the previous discussion, I assumed the diversion rate for the programming that Comcast owns would be the same after the merger as before. However, I now suggest that the diversion rate for the programming being sold will change in two markets due to the merger. In particular, in the Los Angeles and New York designated market areas, Comcast will acquire two RSNs owned or managed by TWC. In these markets, Comcast already owns NBC O&Os. If negotiations for the newly acquired RSNs are bundled with negotiations for the NBC O&Os, and Comcast threatens to withhold both programming assets from its rivals unless its pricing demands are met, then one would expect a larger number of subscribers to leave the rival and potentially go to Comcast. This harm

would be incurred by all MVPDs who operate in the New York and Los Angeles markets, regardless of whether they compete against Comcast.<sup>25</sup>

#### K. Double Marginalization

A final issue relates to an argument Comcast made in the Comcast-NBCU merger review with respect to the double marginalization effect. The claim was made that before the transaction NBCU charged a positive price to Comcast when its marginal cost for selling the programming was near zero, and that after the merger the firm will treat the price as zero, because it is just an internal transfer within Comcast post-merger. This is a standard argument made in a bilateral monopoly situation. But, as accepted by the FCC in the Comcast-NBCU merger, <sup>26</sup> this reasoning overlooked the fact that Comcast competes with other MVPDs for subscribers and makes profits from selling programming to these rival MVPDs. Once one takes account of this added opportunity cost effect, the double marginalization effect is relatively small.

# IV. Horizontal Harms Due to the Merger

There are two sets of horizontal harms created by the merger of Comcast and TWC. The first concerns the addition of TWC's RSNs in Los Angeles and New York City to the vast array of programming offered by Comcast. The second concerns the increased bargaining power that Comcast will have with programmers due increasing its subscriber size from 21 to 29 million.

<sup>&</sup>lt;sup>25</sup> This argument is consistent with the FCC's rulemaking that banned separately owned, same market Big 4 stations form coordinating their retransmission consent negotiations. *Amendment of the Commission's Rules Related to Retransmission Consent*, Report and Order and Further Notice of Proposed Rulemaking, MB Docket No. 10-71, (rel. Mar. 31, 2014), ¶ 6. There, the FCC accepted that prices would be higher as a result of the horizontal consolidation. n I.B. (2011) ("*Comcast-NBCU Order*").

<sup>&</sup>lt;sup>26</sup> Comcast-NBCU Order, 26 FCC Rcd at 4247, ¶ 237, Appendix B, Technical Appendix, Section I.B.

#### A. The Horizontal Harm Due to the Addition of TWC's RSNs.

Under the proposed merger, Comcast will obtain the two TWC RSNs in the two largest cities and media markets of the United States, Los Angeles and New York. In the New York and Los Angeles markets, combining these very valuable assets with the Comcast programming offered there, particularly the two NBC O&O stations, will allow Comcast to raise prices to other MVPDs. In an earlier ruling, the FCC concluded that it was not in the public interest for two of the top four stations in a given geographic area to jointly negotiate retransmission agreements.<sup>27</sup> The FCC found that two separately owned, same market broadcasters who coordinate their retransmission consent negotiations can extract higher prices than when broadcasters negotiate separately. Thus, by adding the very popular RSN in both Los Angeles and New York to the NBC O&O, Comcast would be able to obtain higher prices for both programming than can be obtained today when the programming is negotiated separately. Also, in the Comcast-NBCU merger, the FCC ruled that separate joint ownership of an RSN and local broadcast affiliate would allow the owner to charge higher prices for the programming than if each were owned separately.<sup>28</sup> Accordingly, it is also not in the public interest.<sup>29</sup>

To see how there is horizontal harm in the programming market, take the following example. Suppose an MVPD had the value of \$10 for the first network that it purchased and the value of \$5 for the second network it purchased. Suppose that the negotiated prices give the programmer and MVPD one half of the surplus. If different programmers own the networks, each would be able to get the marginal value of the second network given that the MVPD was going to buy the other network. Then

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<sup>&</sup>lt;sup>27</sup> Amendment of the Commission's Rules Related to Retransmission Consent, Report and Order and Further Notice of Proposed Rulemaking, MB Docket No. 10-71, (rel. Mar. 31, 2014), ¶ 6.

<sup>&</sup>lt;sup>28</sup> Comcast-NBCU Order, 26 FCC Rcd at 4247, ¶ Appendix B, Technical Appendix, Section I.C.

<sup>&</sup>lt;sup>29</sup> Amendment of the Commission's Rules Related to Retransmission Consent, Report and Order and Further Notice of Proposed Rulemaking, MB Docket No. 10-71, (rel. Mar. 31, 2014), ¶ 6.

each programmer would get \$2.50 per network. This will have a total programming cost of \$5 for the two networks. On the other hand, if one programmer possessed both networks, then it could charge for a bundle of the two networks for a price of \$7.50, the value of the network is \$15 and the programmer gets one half of the surplus.

These programming effects do not rely on the networks being close substitutes, but on the fact that the value of additional networks has diminishing value to an MVPD. Suppose that the MVPD valued the first network T and the value for a second network T(1-x), where x is a number between 0 and 1. If the value of x is 0, then the networks have independent marginal values of T each, while if it is 1, the networks are perfect substitutes and the marginal value for each is 0. If the networks are owned separately, then each would be able to get one half their marginal valuations from an MVPD of T(1-x)/2 for a total programming cost of T(1-x). On the other hand, if one programmer owns both networks, then the total value is T(2-x). If the programmer receives one half the value of the network, then it receives T(1-x/2), for an increase in programming costs of Tx/2. So, even if the networks are not close substitutes the combining of assets could lead to substantial cost increases. The FCC agreed with this analysis in the Comcast-NBCU Order. Order. In particular, the FCC's analysis examined the case where a Fox O&O broadcast TV station and a Fox RSN were available in the same local market under the joint ownership of News Corp., relative to a control group of RSNs not under joint ownership with a broadcast station.

Given that both the NBC O&O and the TWC RSNs are considered by the FCC to be "must have" programming, the horizontal harm due to this combination of programming assets is substantial.

<sup>&</sup>lt;sup>30</sup> Comcast-NBCU Order, 26 FCC Rcd at 4247, ¶ Appendix B, Technical Appendix, Section I.C.

 $<sup>^{31}</sup>$  Id

Because Comcast has both of these program forms in the two largest media market in the United States, the potential for harm to all MVPD providers in the markets where the programming is made available will be substantial.

## B. Increased Comcast Bargaining Buying Power in the Programming Market

Comcast will be able to demand lower prices from programmer by growing from 21 million subscribers to 29 million subscribers. The 29 million subscribers is nearly the 30% of the market that the FCC once demarcated as the maximum that any MVPD may have in order to reduce the possibility that if that MVPD refuses to buy the programming, there will be enough remaining MVPDs the programmer can sell to and still be able to cover its costs. I agree with the FCC's historic concerns about buyer concentration in the programming market and that this will lead to lower prices for Comcast.

By obtaining lower prices, Comcast will increase the profitability per subscriber for Comcast and using equation 1, this will lead to an increase in the opportunity cost for Comcast to sell its programs to rival MVPDs. This will lead to higher Comcast programming prices for these MVPDs and these increases in costs will in part be borne by subscribers.

Furthermore, when responding to some critics, Rosston and Topper<sup>33</sup> (paragraph 185) argue:

Comcast would gain market power against content providers because it would be a post transaction "bottleneck" that prevents a network from reaching a national audience and being commercially viable. Comcast will not become

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<sup>&</sup>lt;sup>32</sup> Third Report and Order, In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992: Horizontal Ownership Limits, FCC 99-264; MM Docket No. 92-264 (Released: 20 October 1999).

<sup>&</sup>lt;sup>33</sup> See Footnote 24.

such a "bottleneck" as content providers have a large open field other than Comcast for selling their programming after the transaction.

Rosston and Toper are treating the programming market as if being a large buyer does not increase a firm's market power, because no individual MVPD is essential for any given programmer or broadcaster to profitably be in the market. Unfortunately, in the programming market it is well-known that larger MVPDs get much better programming rates than smaller ones. It flies in the face of reality to think that by enlarging, Comcast will gain no additional market power as a purchaser in the programming market. If Comcast lost market power, and had to pay higher prices, then this would be a very large incentive not to merge with TWC. The merger will lead to higher profitability per subscriber due to the lower costs of buying programs, and again, a higher opportunity cost for Comcast to selling its programs to its competitors.<sup>34</sup> Furthermore, and most strikingly, if TWC and Comcast thought that the merger would mean paying higher programming prices, then they would not allow [[]] This is another piece of evidence suggesting Comcast will get better pricing from programmers as a result of

another piece of evidence suggesting Comcast will get better pricing from programmers as a result of the transaction with TWC and Charter.

It is useful to realize that getting lower programming prices gives exactly the same mechanism for raising the opportunity costs of selling programs to rivals discussed above due to the alleged efficiencies that could arise from the merger.

<sup>&</sup>lt;sup>34</sup> In their arguments on this topic, Rosston and Toper referenced "The Role of Firm Size in Bilateral Bargaining: A Study of the Cable Television Industry" by Tasneem Chipty and Christopher Snyder, Review of Economics and Statistics, (1999) 81(2):326-340. Their study showed that there is a theoretical possibility that merging can hurt a buyer's bargaining power; if the seller's gross surplus selling function is convex and demonstrate that this is often the case in their study. There are problems with using this study. For example, they make an assumption that buyers –MVPDs – do not compete with other MVPDs, which is clearly not true given the overlap between many if not most MVPD coverage areas. The assumption of MVPDs not competing may have been reasonable given that the data set they used ended in 1993, but it is clearly not a reasonable assumption now.

Operators of small cable systems insist, based on their experiences purchasing programming, Comcast obtaining lower prices will result in smaller MVPDs paying higher prices. Empirical data indicate that this is in fact what happens in the marketplace today when programmers do not receive what they expect from Comcast in their negotiations. The data suggest this effect would continue and be made worse as Comcast's bargaining power increases. From an economic standpoint, this assertion can be explained as follows: when publicly held programming firms address market analysts they often promise to achieve a given rate of return in order to convince the analysts to recommend to their clients that they buy the programmer's stock. In other words, they tell a revenue growth story. This is a commitment by the programmer to achieve higher rates of return. If the programmer does not meet Wall Street's expectations, it could lead to a drop in the programmer's stock. It is much more difficult for a programmer to try negotiate a substantial price increase with Comcast than a smaller MVPD, because Comcast is seen as being a "must have" program distributor, whereas a programmer would not be hurt as much if a smaller MVPD did not carry its programs. If the programmer must give Comcast a lower price in return for carriage of its programming, then it must turn to other buyers – the smaller MVPDs – to make up the difference or the revenue-growth story told to Wall Street becomes invalid. This ability to commit to given rates of return provides an economic linkage between the prices paid by rival MVPDs and Comcast.

Finally, some commentators (See, e.g. Wallsten<sup>35</sup>) claim that it is unclear whether the price of programming will increase if Comcast becomes larger, because as Comcast becomes larger, programming becomes more important to it. Wallsten alludes to some work where a firm that obtained

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 $<sup>^{35}</sup>$  An Economic Analysis of the Proposed Comcast/Time Warner Cable Merger by Scott Wallsten, May 2014

more market power actually paid a higher price for an input.<sup>36</sup> The problem with this argument is that the marginal incentives change for the programmer due to Comcast's size but they do not for Comcast. The fact that Comcast becomes larger does not make the programming more valuable, because Comcast receives the same profit per subscriber.<sup>37</sup>

The bottom line is that the largest MVPDs get lower programming prices and this will raise the opportunity costs for selling programs to rival MVPDs.

# V. The Problems with the FCC's Arbitration Remedy

A programming dispute between Comcast and an MVPD could be settled by the MVPD invoking its right to take the dispute to commercial arbitration using the "final offer" or "baseball" style arbitration remedy imposed on Comcast-NBCU by the FCC as a condition of approving the license transfers associated with the merger. Under this form of arbitration, each side presents an arbitrator with a proposed resolution – its "final offer" – and the arbitrator picks the proposal that most closely approximates the "fair market value" of the programming. To improve use of the remedy for smaller MVPDs, the FCC directed that if Comcast's "final offer" is not chosen by the arbitrator, Comcast must pay the winning MVPD's legal costs associated with taking the case to arbitration.

I note that MVPDs who are members of the NCTC generally have the option of opting into the buying group's master agreements at the prices established pursuant to that deal. NCTC currently has a master agreement with Comcast for its national cable programming and for its ten NBC O&O

<sup>&</sup>lt;sup>36</sup> See footnote 35.

<sup>&</sup>lt;sup>37</sup> Wallsten (2014) says that one hypothesis for why Comcast obtains lower prices is that Comcast is in a better position to make long term commitments to programmers than smaller MVPDs. This possible hypothesis has no basis in fact.

<sup>&</sup>lt;sup>38</sup> *Comcast-NBCU Order*, 26 FCC Rcd at 4247, ¶¶49-59.

stations. If an NCTC member expects to opt into the NCTC deal with Comcast, then they would not be expected to negotiate directly with Comcast. NCTC does not have, and has never had, an agreement for Comcast's RSN programming. For this programming, an NCTC member must negotiate with Comcast directly for RSN programming owned by Comcast.

Despite the availability of an arbitration process, even one with special provisions for smaller MVPDs, a smaller operator is unlikely to use it and is therefore effectively lacking any remedy for the recognized competitive harms created by the merger. One reason for this is that smaller MVPDs or the NCTC lack information about the fair market value of Comcast's programming. This leads smaller MVPDs and NCTC to believe their chances of prevailing in arbitration are low. Comcast recognizes that MVPDs that purchase its programming, particularly those that are small or the NCTC, have little confidence in being able to win an arbitration for this reason, and negotiate without fear that the arbitration condition will be invoked against them. This undermines a key reason why the FCC imposes its arbitration conditions: "Our arbitration condition is intended to push parties towards agreement prior to a breakdown in negotiations.<sup>39</sup>" In other words, the MVPD will likely pay a higher price or face less reasonable terms as a result of the Comcast/TWC transactions.

A. Comcast's Informational Advantage Over Other MVPDs, Including Bargaining Agents

In considering whether to utilize baseball style arbitration, the NCTC and/or a smaller MVPD will know only the contracts it has for such programming, and for broadcast and regional sports

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<sup>&</sup>lt;sup>39</sup> *Id.* at ¶ 59. Continuing, the FCC stated: "Final offer arbitration has the attractive 'ability to induce two sides to reach their own agreement, lest they risk the possibility that a relatively extreme offer of the other side may be selected by the arbitrator. We find that the availability of an arbitration remedy will support market forces and help prevent this transaction from distorting the marketplace."

networks. Their knowledge of the market may be even more limited. This will lead the NCTC or smaller MVPDs to believe their chances of choosing a final offer that is close to Comcast's programming's fair market value is low.

This lack of information that an MVPD will have when trying to estimate how an arbitrator will determine the fair market value of programming is multi-faceted. The NCTC or smaller MVPD lack information concerning: (i) the previous prices that Comcast charged to other MVPDs for programming; (ii) how its programming prices varied with MVPD size, that is the size of the "bargaining premium" paid by small MVPDs; and (iii) Comcast's cost of acquiring the programming.

Exacerbating the lack of critical information is that fact that Comcast will likely have more and better information about what is fair market value for the programming that it sells, because it possesses all the contracts that it has with the other MVPDs that carry its programming, and thus the market in general. This gives Comcast a strong advantage over NCTC or a smaller MVPD in how it makes its offer in a baseball-style arbitration process. Because an MVPD or the NCTC will lack the critical information in order to make a viable final offer, and will also know that Comcast will be much better able to make a proposal that will be accepted, there is a low likelihood that either will go to arbitration in the first place. The informational advantage that Comcast has is such a high hurdle that almost no firm, particularly the NCTC or smaller MVPDs, will take it to arbitration as it is currently constituted. It would actually be against the odds for an MVPD to win an arbitration given the informational advantage that Comcast has. These informational advantages favor Comcast and it will be able to act without concerns of being taken to arbitration.

#### B. Other Problems with the Arbitration Process

There are other reasons why the arbitration process is stacked against smaller MVPDs. First, an MVPD has to have the ability to finance the cost of arbitration. For a small firm this is not necessarily an easy thing. The legal costs of arbitration can be quite high about \$1 million, and the process may take many years to reach a resolution. For a small MVPD with relatively low capitalization, the liquidity constraints that it may face may make the possibility of fronting this legal cost infeasible. Therefore, the option to take on a very well-capitalized firm such as Comcast is not possible no matter how strong its case is and no matter how large the potential gain that it expects to achieve through arbitration. That is, even if a small MVPD is convinced with probability one that it will win the case and eventually be compensated for all its legal fees, it will not be able to afford to bring the case no matter how badly Comcast is treating the MVPD.

Second, most of the smaller MVPDs are not publicly traded corporations and for their major, the investment represents a large portion of their portfolios. If this is the case, the firm is likely to behave in a risk-averse manner. This implies that the owners of these companies have a low tolerance for risk. This will make it less likely to go to arbitration, because it faces a chance of a very bad outcome of losing the arbitration, facing the fee increase and paying all the legal fees it incurred in the arbitration process.

Finally, because Comcast will be negotiating with every MVPD and possibly face arbitration with each of them, it has an incentive to establish a reputation of being very difficult to take to the arbitration process. It has both the ability and incentive to spend vast amounts of resources in terms of time and money if it is taken to arbitration in order to signal to all MVPDs that the arbitration process will be very costly. Comcast is likely to do this, and this will be observed by all the other MVPDs, greatly reducing their incentives to engage in the arbitration process with Comcast which is exactly

what Comcast would like. Comcast has an incentive to punish an MVPD for taking it to arbitration. It wants a reputation of being tough so that other MVPDs do not challenge Comcast in arbitration.

### C. Algebraic Representation of Process

I will now show algebraically, that even without the above concerns, the arbitration process as it is currently designed is inadequate for smaller MVPDs. Even assuming that the MVPD believes it has a 50/50 chance of winning the arbitration, and it has one-way fee shifting, a smaller MVPD still will not utilize the arbitration condition. Thus, either stronger arbitration conditions or some other mechanism needs to be provided to deal with the imbalance between Comcast and these smaller MVPDs. This will help explain why no small MVPD has taken Comcast to the arbitration process since the merger.

Suppose that an MVPD and Comcast are in a dispute and the MVPD is thinking of taking Comcast to arbitration. Assume that the length of time of the programming contract that is under dispute is three years. The amount of money per subscriber per month that Comcast is demanding above what p that the MVPD thinks is appropriate is  $\Delta p$ . The number of subscribers that the MVPD has is s and the probability that the MVPD thinks that it will win in arbitration is q. Finally, assume that the MVPD's expected legal costs are L.

The MVPD's costs if it does acquiesces to Comcast's demand of a price of  $p+\Delta p$  and not go to arbitration is

$$(p + \Delta p)*36s$$

This is the three-year cost of complying with Comcast's demand.

If the MVPD takes Comcast to arbitration, then its expected cost is

$$q(36ps) + (1-q)[(p + \Delta p)36s + L].$$

The first term is the probability that the MVPD wins the arbitration, q, times the annual cost of the MVPD's offer. By winning the arbitration, the MVPD does not have to pay  $\Delta p$ , the increase demanded by Comcast or its legal fees. The second terms represent the probability that the MVPD loses in arbitration times the costs in fees paid to Comcast  $(p + \Delta p)36s$  plus its legal fees, L.

Taking Comcast to arbitration is better for the MVPD if and only if

$$(1-q)L \leq 36sq\Delta p$$
.

This says that the MVPD will consider taking Comcast to arbitration only if its expected legal costs do not exceed its expected cost of acquiescing to Comcast's, from the MVPD's point of view, unreasonable demands.

Next, I present a realistic example of parameter values. Suppose that the MVPD has 10,000 subscribers, s, the price increase demanded by Comcast is .25,  $\Delta p$ , the probability that the MVPD expects to win the arbitration case is 50%, q, and the expected legal costs that the MVPD expects to incur are \$1 million. Assume that the MVPD thinks the proper price for Comcast's service should be a dollar (\$1.00), the value of p. Then the MVPD will not take Comcast to arbitration, because

$$(.50) * (1,000,000) = 500,000 > 45,000 = 36 * (10,000) * (.50) * (.25)$$

Thus, even though the MVPD thinks it has a 50% chance of winning in arbitration, there is one-way fee shifting, and the price increase is 25 cents, or 25% above what the MVPD thinks is the

appropriate price for the services that Comcast is providing, it is not a rational decision for the MVPD to take Comcast to arbitration.

Another way to think about the cost of arbitration is to look at the legal costs as a fraction of the per-subscriber payments. In the example above, there are 10,000 subscribers and the legal cost of arbitrating is a million dollars. Thus, the legal costs are equivalent to 100 dollars per subscriber.

Amortized over a year, this would be equivalent to a monthly fee of \$2.77 per month per subscriber even when amortized over 3 years.

This example\_is actually conservative with respect to the costs an MVPD faces when thinking about arbitration. It does not include any of the non-pecuniary costs that a firm will incur when going through arbitration, such as senior management opportunity costs. The arbitration process, together with any appeals, can last for years and require an enormous amount of executive time. Clearly, for medium and small MVPDs, this is a substantial amount of capital.

# VI. Conclusion

In this paper, I demonstrated that the Comcast-TWC-Charter transactions will cause harm to subscribers in the video market. The transactions exacerbate the harms that were caused by the 2011Comcast-NBCU merger. The incremental harms include the increased vertical harm due to Comcast's increased overlap with many rival MVPDs. Also, there increased horizontal harms to consumers due to Comcast adding TWC RSNs in Los Angeles and New York and the increased buying power that Comcast will have in the programming market. Both of these effects will increase Comcast's opportunity cost of selling its programs to rival MVPDs and thus will raise the price to the MVPDs and part, if not most, of this increase will be passed on to their subscribers. The arbitration

conditions that were initiated for small and medium-sized MVPDs and their bargaining agent to buy

Comcast programming following the merger of Comcast and NBCU were not sufficient to protect

these buyers and will be even more inadequate to remedy the harms of the proposed transactions.

# EXHIBIT B

# Before the Federal Communications Commission Washington, D.C. 20554

In the Matter of	)	
Applications of	)	
Comcast Corp.,	)	
Time Warner Cable, Inc.	)	MB Docket No. 14-57
Charter Communications, Inc., and	)	
SpinCo	)	
	)	
For Consent to Transfer Control of	)	
Licenses and Authorizations	)	

### **DECLARATION OF RICH FICKLE**

- 1. My name is Rich Fickle. I am Chief Executive Officer and President of the National Cable Television Cooperative (NCTC). My business address is 11200 Corporate Avenue, Lenexa, Kansas, 66219.
- 2. I have been with the NCTC since 2011. In my role, I oversee all operations of NCTC, including the negotiation, execution, and renewal of all content agreements with programmers. I have been working in the cable/media industry for over 25 years. Prior to my role at NCTC, I was involved in the negotiation of programming rights for new forms of distribution using advanced technology, and involved in programming-related decisions as a VP for a cable operator.
- 3. NCTC is a non-profit cooperative purchasing organization for its member companies that own and operate cable systems throughout the United States and its territories.

  Almost all small and medium-sized multichannel video programming distributors (MVPDs) are members of the NCTC, which currently has approximately 910 member companies serving

millions of MVPD subscribers. NCTC member companies differ in size. The largest serves millions of subscribers and the smallest serves tens of subscribers. The member-size median is fewer than 1,500 subscribers. NCTC members include traditional cable companies, traditional telephone companies offering video, municipal video providers, and Indian Tribes offering video service.

- 4. NCTC functions as a buying group, negotiating standardized master agreements with programmers and technology vendors. NCTC acts as an interface between the vendor and individual MVPDs so that the vendor can deal with a single entity for purposes of negotiating contracts, determining technical standards, billing for payments, collecting payments, and marketing. These acts provide efficiency to the supplier because they reduce the transaction costs of dealing separately with hundreds of small and medium-sized MVPDs so that the costs are comparable to the transaction costs of dealing with a single large MVPD. MVPDs benefit because they receive lower rates and better terms and conditions than they would receive through direct deals.
- 5. Small and medium-sized MVPDs generally license most of their programming through the NCTC. NCTC has master agreements with the vast majority of cable networks. The largest four members of the NCTC are not actively engaged in NCTC agreements aside from a few minor programming agreements and therefore are considered by NCTC to be inactive.
- 6. Excluding its four largest members, many of NCTC's member companies compete across the country with the largest MVPDs, specifically Comcast, Time Warner Cable and Charter. NCTC members principally compete against larger MVPDs by providing superior customer service, which is often driven by being locally owned and operated. In addition, some

members compete by being faster to embrace technology innovation where possible (e.g. fiber-to-the-home and IPTV).

- 7. I believe that if the Comcast/TWC/Charter deal is approved, programming vendors will receive less value for their programming in the near and long term from the combined companies than they would receive if the companies remained under separate ownership and control. This will happen for three reasons. First, to the extent permissible, Comcast will bring the TWC systems under its existing programming agreements where the persubscriber price paid by Comcast is lower. This will result in the programmers receiving less revenue from the TWC systems than they receive today. Second, as a result of growing from 21.1 million to up to 31.4 million video subscribers (to the extent Comcast negotiates on behalf of Bright House Networks and Midcontinent), Comcast will be in a better position to harm programmers by withholding or threatening to withhold access to its increased subscriber base. Accordingly Comcast will be able to obtain lower programming prices from its programming suppliers. Third, as a result of Charter's subscriber base growing from 4.2 million to up to 8 million subscribers (to the extent it negotiates on behalf of SpinCo), Charter will also have more bargaining power against the programmers, and be able to command better rates, terms and conditions from programmers.
- 8. As a result of Comcast's and Charter's ability to pay less for programming, I expect the largest programming/media companies which have significant bargaining leverage—will extract higher fees and more onerous terms and conditions from other MVPDs in the market and NCTC. There is already a significant difference between the programing fees paid by Comcast and those paid by NCTC members, and I expect the Comcast/TWC/Charter deal will significantly increase this difference.

- 9. I see this seesaw effect play out in the market today. Currently, NCTC faces increased demands from programmers resulting from the concessions that they grant large MVPDs such as Comcast and TWC. Programmers acknowledge during negotiations with the NCTC their need to make up the revenue amounts they are not able to secure from Comcast, TWC or other large MVPDs. Specifically, some programmers have stated their intention to make up lost revenues resulting from their negotiations with Comcast, TWC or others directly through their agreements with NCTC members and other small MVPDs. There is no reason to believe that programmers won't continue to seek concessions from NCTC to make up for the increase in lost revenues after the Comcast/TWC/Charter deal is approved. The Comcast/TWC/Charter merger will put programmers in an even worse position in their negotiations with Comcast and Charter. This is why I expect programmers to make up revenues on the backs of small cable operators in the event the Comcast/TWC/Charter deals are approved.
- 10. Because our members' video footprint currently overlaps with Comcast by a significant amount, Comcast has an incentive and ability to charge the NCTC and its members higher prices for its programming than it would charge NCTC if none of its members competed with Comcast. The same is true with regard to Discovery and Starz, which are attributable to Charter. Due to Charter's competitive overlap with NCTC members, these programmers have an incentive to seek higher prices.
- 11. During our most recent renewal negotiations with Comcast/NBCU at the end of 2012, NCTC considered utilizing the "baseball-style" arbitration condition the FCC imposed on Comcast when it acquired NBCU. NCTC had reason to believe that Comcast/NBCU was not offering us fair market rates, terms, and conditions. However, after careful consideration, NCTC decided that the arbitration condition was inadequate and ineffective, even with one-way fee

shifting in the event we won, to address, the unfair demands of Comcast/NBCU. Following are a few reasons that the condition was inadequate and ineffective.

- 12. First, NCTC did not feel it could reasonably evaluate its likelihood of success in an arbitration proceeding because we lacked critical information on key factors that an arbitrator would likely use to make its determination of fair-market value. Without this information we could not make an informed "final offer."
- possessed information on the prices it currently and formerly charged other MVPDs for its programming. It also knew the prices it granted to larger MVPDs as opposed to smaller MVPDs, and what other programmers charged for similar programming, particularly with regard to broadcast stations due to the fact that Comcast operated as an MVPD in dozens of designated market areas. We knew with all of this information available to them, they would be able to more accurately calculate a fair market value and provide it as its "final offer." Moreover, an arbitrator would find the information that Comcast had highly probative, and would likely rely upon it in determining which of the parties' "final offer" is closer to fair market value. Having access to this information in advance of making a "final offer" gives Comcast a huge advantage and makes their chances of winning higher than ours. This information imbalance exacerbates NCTC's problem of a lack of information as described above.
- 14. NCTC also recognized that it would incur significant costs if it pursued arbitration. From our understanding, and based on our own due diligence in examining use of the arbitration condition, the average cost of baseball-style arbitration is approximately \$1 million. This represents a significant cost compared to both NCTC's annual operating budget and our best guess at how much Comcast was charging us above the fair market value of the programming.

- 15. The lack of critical information to make an informed "final offer," the fact that Comcast had the information it needed to make an informed "final offer," and the costs and uncertain time frame made arbitration an unworkable solution. In sum, NCTC perceived the risks and costs of baseball-style arbitration to outweigh any potential benefits that may result from the arbitration. For these reasons, in our negotiations with NBCU, although we felt we were being overcharged, we did not take advantage of the baseball-style arbitration condition. We just agreed to the final prices, terms, and conditions demanded by Comcast/NBCU.
- 16. Without adequate remedies, consumers and competition will suffer from the Comcast/TWC/Charter deals. First, allowing the programming fee difference between large and small MVPDs to grow will hinder the ability of smaller MVPDs to compete with both Comcast/TWC and Charter/SpinCo. Second, allowing programming fees for smaller operators to rise due to this merger will result in further loss of video margins, and this will reduce their ability to make additional investments in rural markets to deploy advanced broadband and new services. Third, smaller independent programmers will be less likely to reach viable scale without obtaining carriage at reasonable terms from Comcast/TWC and Charter/SpinCo, which may have the effect of reducing diversity in the programming market.
- 17. Finally, with so many subscribers, Comcast/TWC and Charter/SpinCo will be in a better position to drive standards for video distribution technologies with programmers, which could result in their settling on standards that are better for Comcast and Charter but much more costly for small and mid-size cable operators to implement, further exacerbating their inability to compete. In addition, the combined entity can invest in large R&D efforts resulting in unique technology and service offerings not available to smaller operators. Many existing technology

vendors will have fewer opportunities for growth and therefore will tend to reduce R&D spending. The market appeal for new technology suppliers may also be dampened.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct to the best of my information and belief.

Executed on August 25, 2014.

Rich Fickle

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